Ray Dalio says magnificent seven are 'fairly priced'

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Highlight: While some of Bridgewater's readings look frothy, "we do not see bubbly conditions in aggregate", the billionaire hedge fund founder said.

Body

Ray Dalio says his simple answer for investors asking if US equities overall or the magnificent seven mega-cap technology stocks in particular are in a bubble is "no".

In a post on LinkedIn, the billionaire founder of Bridgewater Associates said he used six criteria to define a market bubble, and while some of the criteria were elevated, most were not.

"When I look at the US stock market using these criteria, it - and even some of the parts that have rallied the most and gotten media attention - doesn't look very bubbly. The market as a whole is in mid-range (52nd percentile)."

Link to Image

Sam Mooy

Current market levels, Mr Dalio also said, "are not consistent with past bubbles".

Mr Dalio said *the magnificent seven had driven a meaningful share* of the gains in US equities over the past year. The market cap of the basket has increased by more than 80 per cent since January last year, and these companies now constitute more than 25 per cent of the S&P 500 market cap.

"The Mag-7 is measured to be a bit frothy but not in a full-on bubble. Valuations are slightly expensive given current and projected earnings, sentiment is bullish but doesn't look excessively so, and we do not see excessive leverage or a flood of new and naïve buyers. That said, one could still imagine a significant correction in these names if generative AI does not live up to the priced-in impact."

Mr Dalio also said each of the six criteria he used was measured using a number of statistics, adding that he would not detail how his indicator was constructed because that was proprietary.

Growth predictions

Still, Mr Dalio said one key metric was assessing how high prices were relative to traditional measures.

"Looking at the Mag-7, we are reading Alphabet and Meta as somewhat cheap, and Tesla as somewhat expensive. We'd call the group in aggregate fairly priced.

"This value read is partly based on analyst expectations for growth, so we are assuming that analysts are making reasonable predictions for growth driven by generative AI. This is an area where we have lower confidence because there is so much inherent uncertainty and because it is not our area of expertise."

Mr Dalio also said the indicator looked at whether prices were discounting unsustainable conditions, which calculates the earnings growth rate that is required to produce equity returns in excess of bond returns.

"Currently, this indicator is just around the 67th percentile for the aggregate market - more elevated than some of our other readings. The earnings growth discounted in stocks is still a bit high."

However, Mr Dalio pointed to *Nvidia* and compared it to ***Cisco*** during the dotcom bubble.

"Nvidia's two-year forward [price/earnings ratio] is around 27 today, reflecting that, even as the market cap has grown about 10 times, earnings have also grown significantly and are expected to continue to grow over the next year or two because of actual orders that we can validate. During the tech bubble, ***Cisco***'s two-year forward P/E hit 100. The market was pricing in far more speculative/long-term growth than we see today."

Mr Dalio said that was generally true for the rest of the mega-cap techs: over the past couple of years, the market cap of these companies had grown largely in line with earnings, which had increased rapidly.

"Trading in the Mag-7 (based on turnover) remains near all-time highs in dollar terms, but as a share of the total market cap, it doesn't look like a speculative frenzy," he said.

Mr Dalio said *in terms of sentiment*, another criteria, "the market is now neutral to slightly positive-not in bubble territory".

Graphic

Ray Dalio sees no bubbles at current levels.

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