Bubble, bubble, toil and trouble

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You'll go far to find a more considered voice in the world of investing than Jeremy Grantham (82), co-founder and chief investment strategist of Boston-based asset management company GMO.

I will never forget reading a one-pager he published nearly 12 years ago – probably the best and most prescient piece of commentary on financial markets I've encountered in my career.

Under the title "Reinvesting When Terrified", Grantham urged investors to start deploying cash back into the stock market "in a few large chunks".

The timing of this piece could not have been better: after months of heavy declines in the wake of the global financial crisis, the S&P 500 eventually bottomed out on March 9 2009 (as measured by closing prices); Grantham's piece happened to be published the very next day. Equity markets in the US and elsewhere have risen more than fivefold since then.

It is therefore rather chilling when the very same commentator holds up his hand at the beginning of 2021 and warns that the long bull market has finally matured into a "fully fledged epic bubble".

A couple of weeks after making this statement, the founder of GMO got a chance to explain his thinking on Bloomberg TV.

When I came across the recording, I called my dog and took him for a long walk while listening to every word of the interview. I'm not sure how much of it may have related to the gloomy London weather in mid-January, but I was ready to slash my wrists an hour or so later when I returned home after listening to the depressing outlook.

There was certainly a lot of food for thought.

But I could not help thinking back to a similar experience in May last year: another guru from the investment world, Stanley Druckenmiller, had just given a talk to the Economic Club of New York. The renowned hedge fund manager explained why he believed the rapid recovery in stock prices following the market crash in March 2020 had been totally overdone and was simply not sustainable.

Even though the springtime weather in London was rather pleasant that particular afternoon, I also considered slashing my wrists following a dog walk during which I listened to the Druckenmiller podcast.

I did, however, live to tell the tale – thankfully, I never slashed my wrists. Neither did I sell any shares, even though the wave of pessimism that prevailed made it sound like a pretty tempting idea to lighten one's exposure to risk assets at the time (in the eight months since then, equity indices around the world have increased between 30% and 40%).

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Staying with the theme of pessimistic pronouncements, JPMorgan published a report titled "The Armageddonists" in November 2019 (around the same time the very first case of coronavirus was traced back to the Hubei province in China).

In this piece of research, it tracked some of the most bearish calls by a number of renowned investment professionals over the previous decade or so. The first individual it focused on is Nouriel Roubini, who famously predicted the US housing bubble and ultimate crash in 2007-2008. Not convinced by the subsequent recovery, Dr Doom (as he is affectionately known) lost faith in equities within about a year of the 2009 market bottom.

The list further includes one of the most revered hedge fund managers ever, George Soros, who had this to say at the beginning of 2016: "When I look at the financial markets, there is a serious challenge, which reminds me of the crisis we had in 2008."

One more example: Nobel prize winner Paul Krugman, commenting on the US election result in November 2016, said: "It really does look like President Donald J Trump, and markets are plunging ... So we are very probably looking at a global recession, with no end in sight. I suppose we could get lucky somehow. But on economics, as on everything else, a terrible thing has just happened."

Clearly the opportunity cost would have been vast if one had listened to any of these experts and followed their advice at the time.

Fortunately, I did not yet have a dog in those days, so there were no long walks in the park listening to podcasts spewing gloom and doom.

The lesson from all of this, I guess, is that even the gurus don't necessarily have the answers.

Much as I will always respect Grantham, I would therefore also suggest that one should bear this in mind when considering his most recent warning: he may yet be proved right, and we may indeed be in an epic bubble which is about to burst. But only time will tell. **x**

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