Warren Buffett's favorite market gauge hits 171%, signaling stocks are overheated and a crash may be coming

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Warren Buffett. Bill Pugliano / Getty

- **Warren Buffett's favorite yardstick for stocks is signaling they're overvalued and could crash.**
- **The Buffett Indicator has surged to 171% as investors bet on AI, rate cuts, and a soft landing.**

- **The famed investor has touted the gauge as "probably the best single measure" of stock valuations.**

Warren Buffett's favorite market gauge is flashing red, signaling that US stocks are overpriced and in danger of plunging.

The Buffett Indicator surged to 171% as of Friday's close. Buffett suggested in a Fortune article in 2001 that stocks would be fairly valued at a 100% reading, and buying them at the 70% or 80% level would probably work out nicely. However, he warned it would be "playing with fire" to purchase them around the 200% mark.

The famed investor and Berkshire Hathaway CEO also hailed his namesake indicator as "probably the best single measure of where valuations stand at any given moment." He noted that when the gauge skyrocketed during the dot-com bubble, it should have been "very strong warning signal" of an approaching crash.

Buffett's preferred yardstick takes the total market capitalization of all actively traded US stocks, and divides that figure by the latest official estimate for quarterly gross domestic product (GDP). Investors use it to compare the overall value of the stock market to the size of the national economy.

The Wilshire 5000 Total Market Index has jumped 22% this year, lifting its market capitalization to $46.32 trillion as of Friday's close — its highest level since March 2022. Its gains have been fueled by a 19% rise in the S&P 500 and the Nasdaq Composite's 37% surge this year — as investors bet on an AI boom, cuts to interest rates, and a soft landing for the economy instead of a recession.

Meanwhile, the Bureau of Economic Analysis' advance estimate of second-quarter GDP is $26.84 trillion, which puts the Buffett indicator at 171%. The measure proved its worth last year, when it plummeted from over 210% in January to below 150% by September.

However, it's worth emphasizing that Buffett's go-to gauge isn't flawless. For example, it compares the stock market's current value with a past estimate of economic output. GDP also excludes overseas income, whereas US companies' market caps reflect the value of both their domestic and foreign operations.