Can the US equity market cause the next global financial crisis?

Are a few American tech giants, like the Pied Piper of Hamelin, leading global investors into the river — hypnotized by the tune of innovation, only to risk drowning in overvaluation?

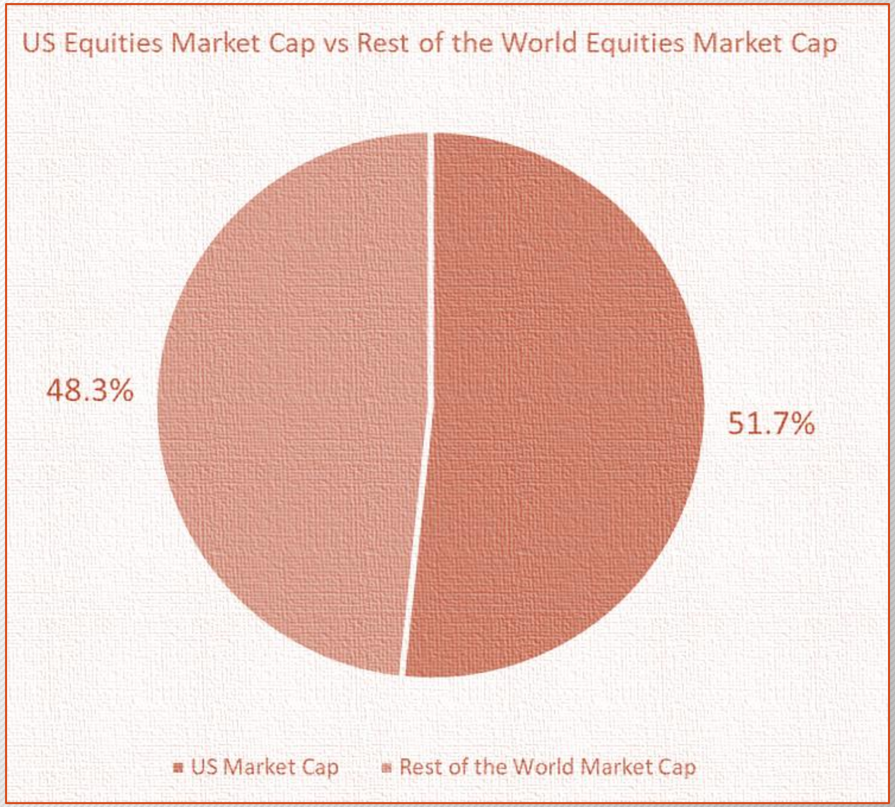
Context

- An article by Gita Gopinath (Professor of Economics at Harvard University and Ex-Chief Economist and Deputy MD at IMF) published in the economist, has gained a lot of attention as it claims that the next US equity markets crash could lead to $35 trillion in loss of value for investors globally. The large number, which represents about 30% of global GDP and about 25% of global equity market capitalisation, has attracted significant media attention.
- Gita makes the case that more US retail investors (directly or via ETFs) are now invested in US equity markets than ever before and US equity markets have become a bandwagon for global investors especially post covid. Foreign investors have more than $60t invested in US treasuries, equities and other asset classes. Fate of the rest of the world, is intricately linked to what happens to US economy and its various asset markets.
- In the following pages, we examine various data points to see how likely are we to a potential crash and whether such a crash can have a global impact.

Are US equity markets in a bubble?

US Economy is about 26% of Global GDP, whereas its equity markets are at about 52% of global equity markets

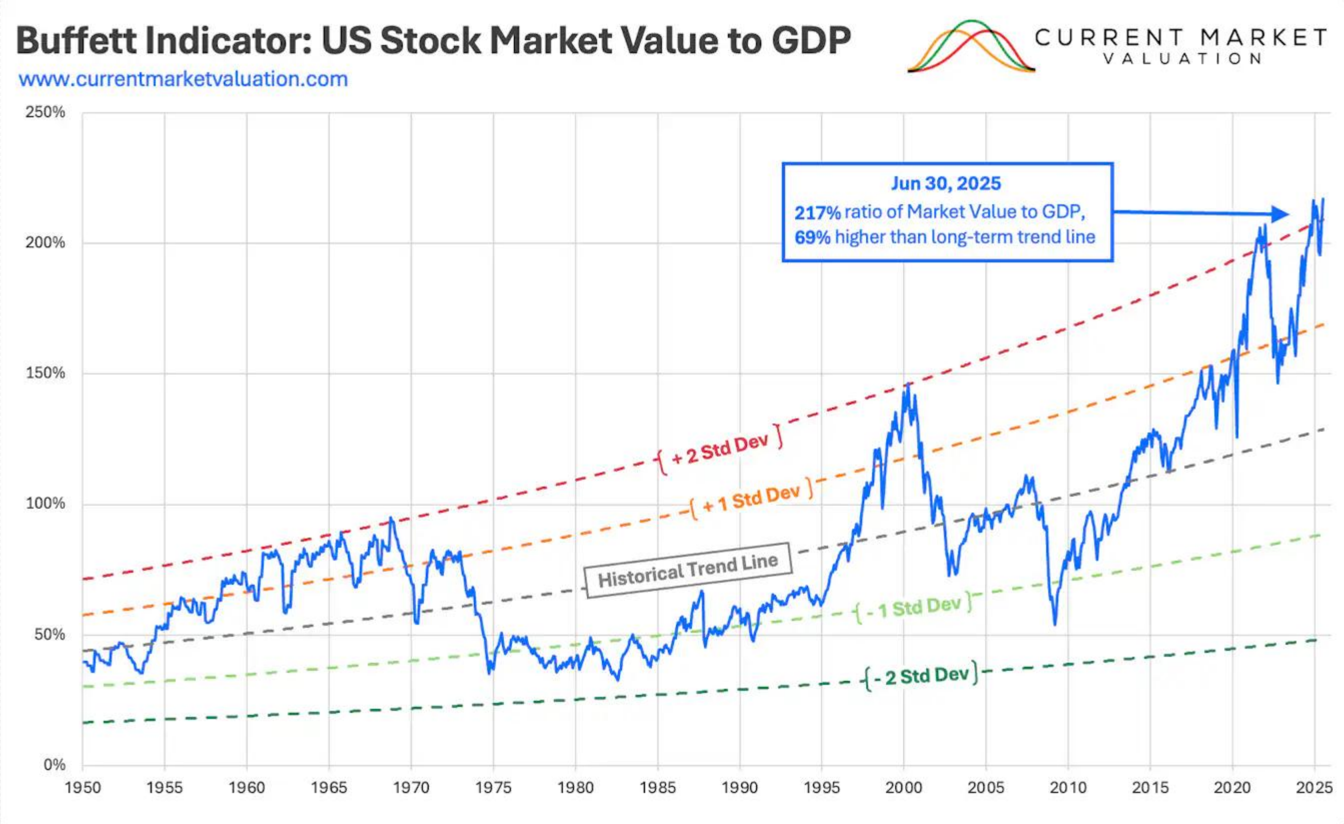
The U.S. now represents over half of the world's total stock market value. This means a severe downturn is no longer just an American problem. It has become, by definition, a global event that directly impacts every investor on the planet.



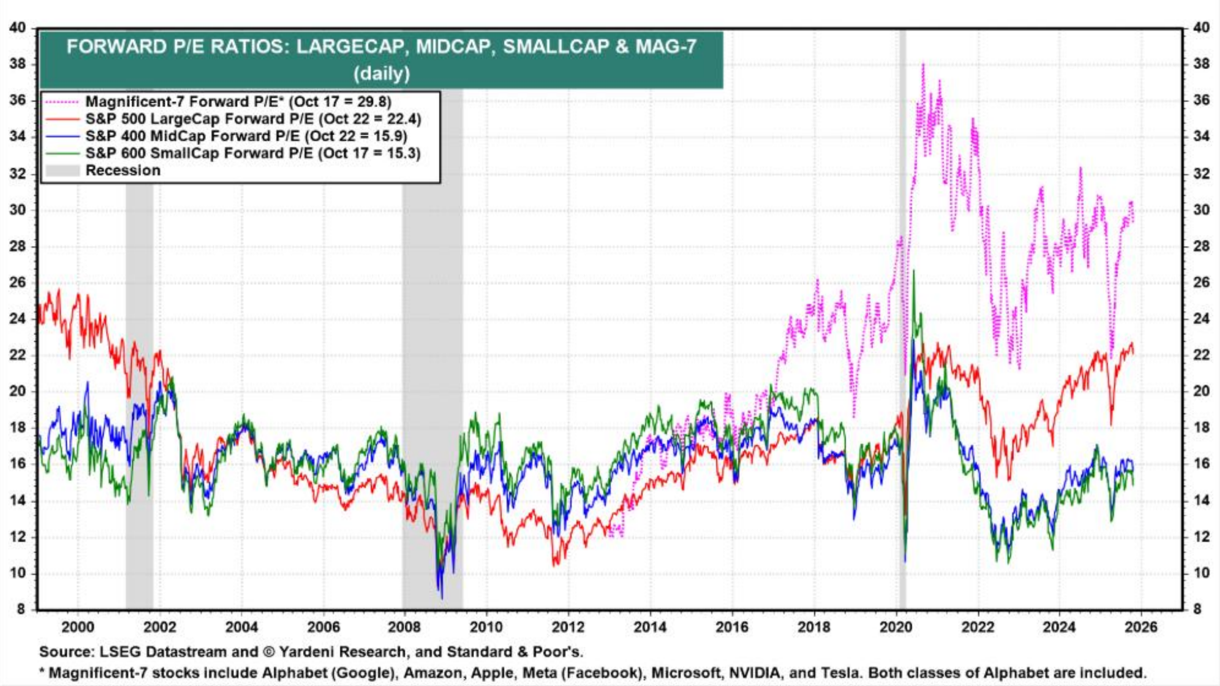
US equity market capitalization as a % of US GDP an all time high of 217% has rung alarm bells ..

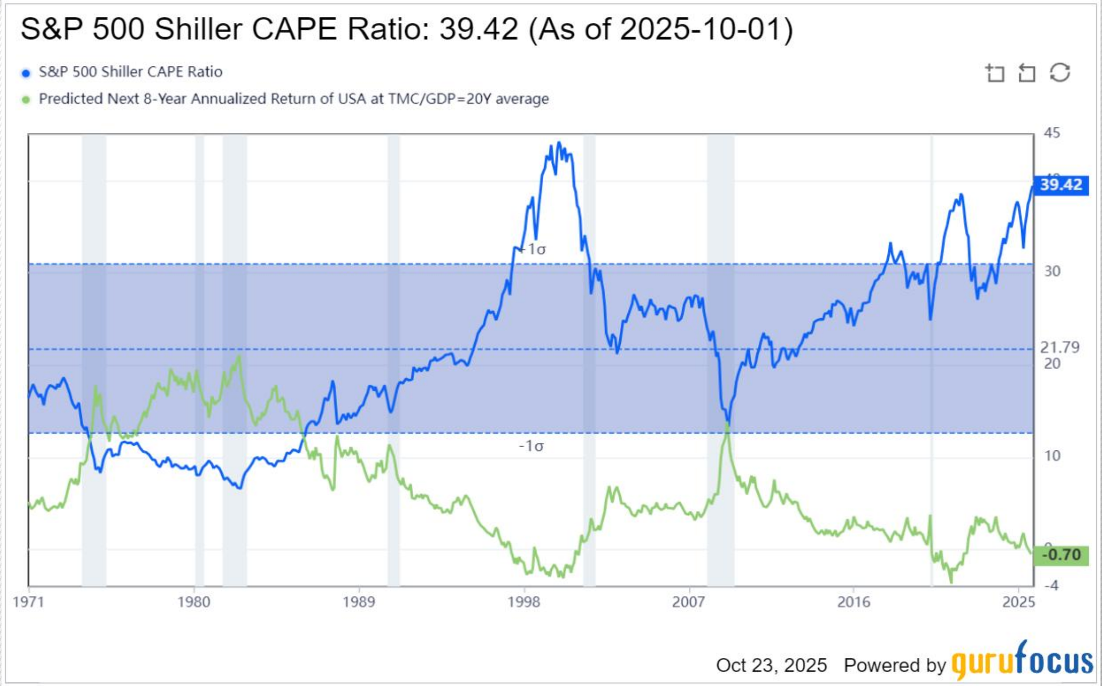
Equity investors continue to pour money into US equity markets despite the Buffett indicator at all time highs. Most investors believe that they can dance close to the door and will be first to exit!

It is also noteworthy, that majority of the valuation gains are coming from AI led themes and interest rates are no longer near zero as was the case, post GFC till 2023.



Earning multiples at record highs and CAPE ratio nearing 1999 tech bust period..

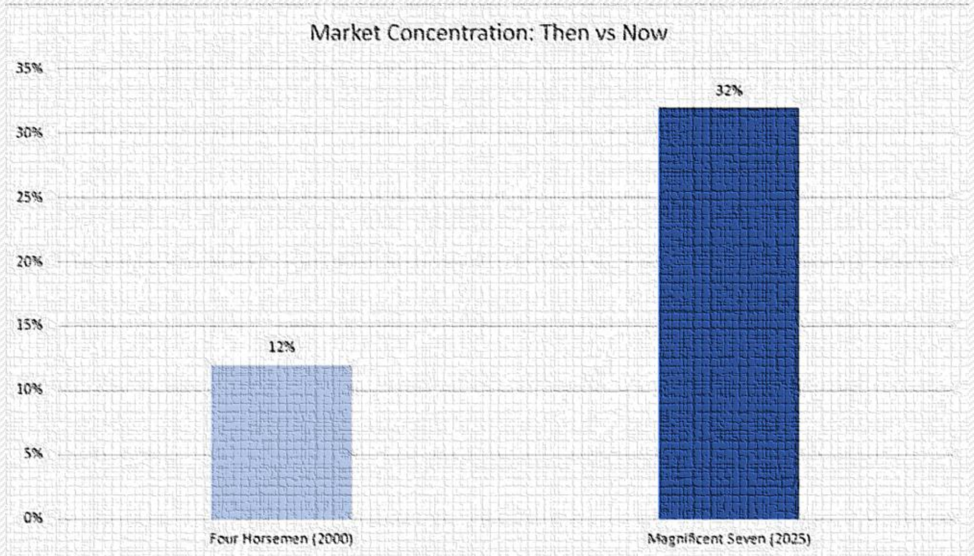




Magnificent Seven are trading at a Forward P/E of nearly 30x, a steep premium over the broader S&P 500 at 22x. This isn't just growth; it's a market "priced for perfection," where investors are paying today for years of flawless execution and continued hyper-growth in the future. This high valuation leaves no room for error. Any sign that these companies' growth is slowing to a more normal rate could trigger a severe re-rating of their stock prices.

Shiller CAPE ratio is near 40x, a level of extreme valuation only seen twice before in U.S. history: just before the Great Depression and at the peak of the dot-com bubble. Both prior instances were followed by devastating market crashes.

Illusion of diversification

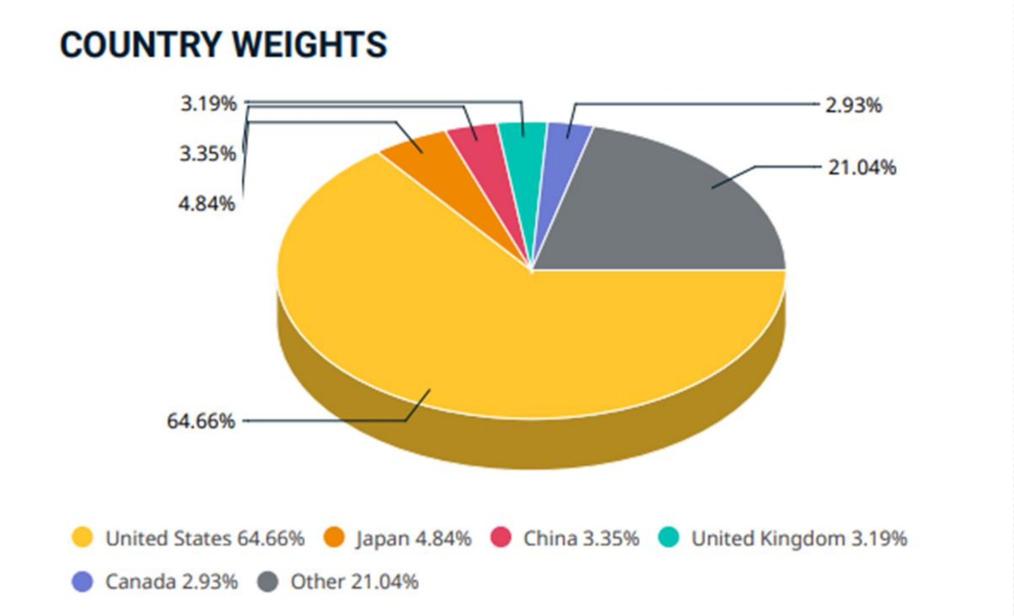


The market concentration has nearly tripled from 2000s Dot-Com peak to the AI generation while the rally still continues today. This is no longer a sectoral risk, instead it poses a risk to the entire market. This extreme concentration creates a dangerous illusion of diversification. Millions believe their S&P 500 ETFs are safely spread across the economy, but they are unknowingly making a massive, concentrated bet on a single sector.

Rest of the World, hitching to the American bandwagon

Creating the global contagion risk, once again

One Country & One Sector concentration in global indices



Top 10 Constituents

Constituent	Country/Market	ICB Sector	Net MCap (USDm)	Wgt %
Nvidia	USA	Technology Hardware and Equipment	4,358,085	4.76
Microsoft Corp	USA	Software and Computer Services	3,833,721	4.19
Apple Inc.	USA	Technology Hardware and Equipment	3,704,826	4.05
Amazon.Com	USA	Retailers	2,102,072	2.30
Meta Platforms Inc	USA	Software and Computer Services	1,600,247	1.75
Broadcom	USA	Technology Hardware and Equipment	1,520,600	1.66
Alphabet Class A	USA	Software and Computer Services	1,410,286	1.54
Tesla	USA	Automobiles and Parts	1,248,436	1.36
Alphabet Class C	USA	Software and Computer Services	1,150,441	1.26
Taiwan Semiconductor Manufacturing	Taiwan	Technology Hardware and Equipment	1,039,574	1.14
Totals			21,968,290	24.00

FTSE Global

TOP 10 CONSTITUENTS

	Country	Float Adj Mkt Cap (USD Billions)	Index Wt. (%)	Sector
NVIDIA	US	4,552.55	5.04	Info Tech
APPLE	US	3,803.11	4.21	Info Tech
MICROSOFT CORP	US	3,657.20	4.05	Info Tech
AMAZON.COM	US	2,097.93	2.32	Cons Discr
META PLATFORMS A	US	1,594.45	1.77	Comm Srvcs
BROADCOM	US	1,474.14	1.63	Info Tech
ALPHABET A	US	1,414.84	1.57	Comm Srvcs
TESLA	US	1,289.18	1.43	Cons Discr
ALPHABET C	US	1,196.59	1.33	Comm Srvcs
TAIWAN SEMICONDUCTOR MFG	TW	1,054.86	1.17	Info Tech
Total		22,134.84	24.52	

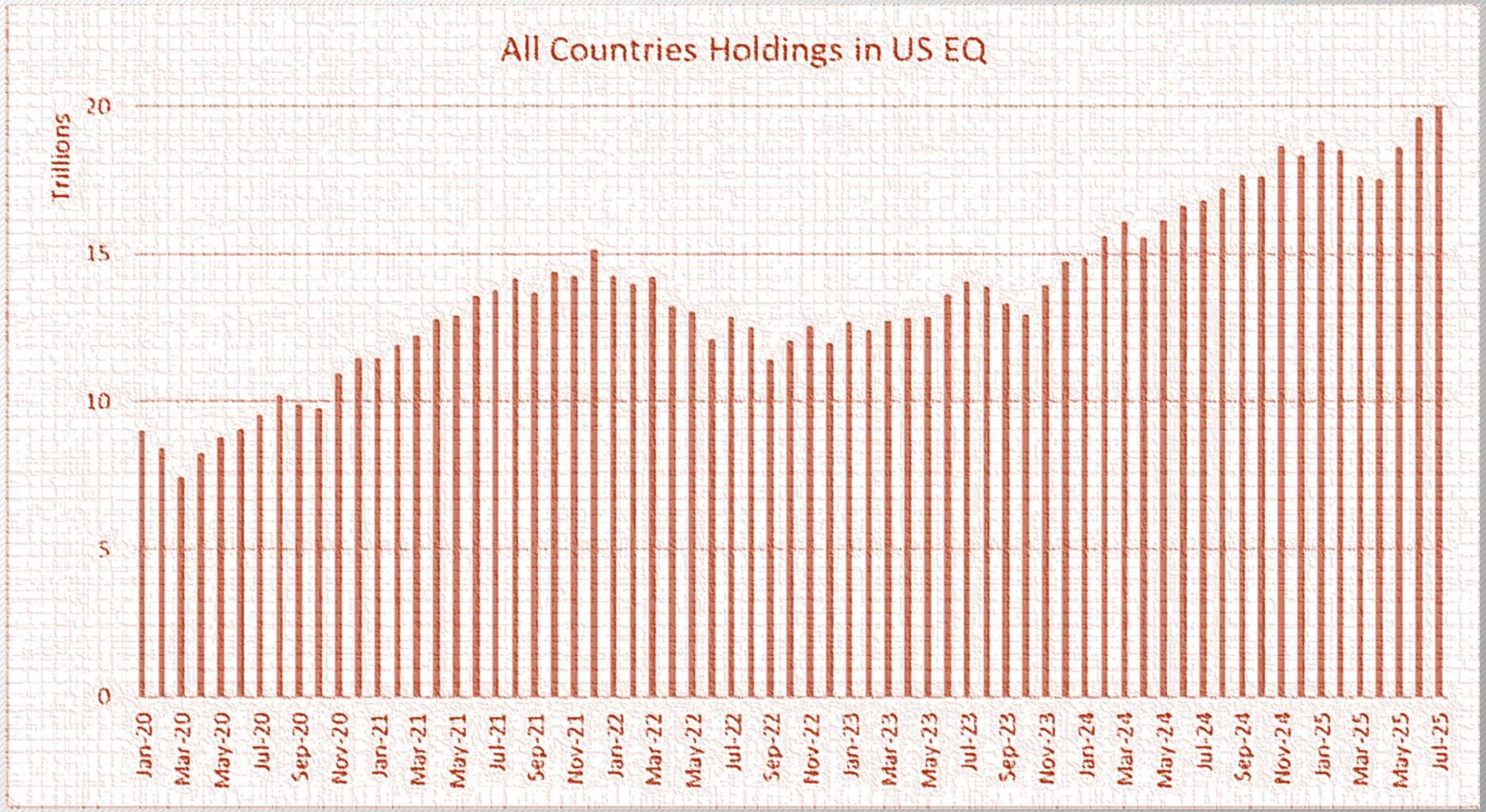
MSCI ACWI

With the top 10 companies making up nearly a quarter (24.5%) of the entire global index, a "global" investment is no longer diversified. It has become, by default, a massive, concentrated bet on the performance of a few U.S. tech giants.

Rest of the World has $20t riding on US equity markets, an all time high and almost double since 2020..

Since 2020, foreign holdings in U.S. equities have more than doubled, exploding from $9 trillion to nearly $20 trillion. This represents a compound annual growth rate of 15.1%, a staggering pace that highlights the world's unprecedented exposure to a U.S. market downturn.

“Foreign investors could face wealth losses exceeding $15trn, or about 20% of the rest of the world’s GDP.”
-Gita Gopinath



Source – U.S. Dept of Treasuries

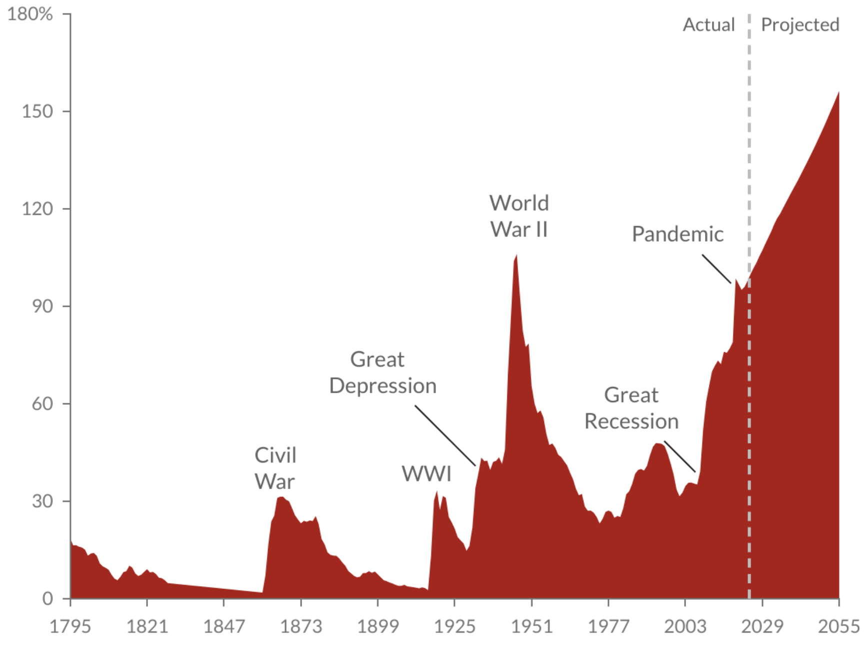
Can the Fed bail out US & Global equity investors?

Does the Fed have any new keys to open these handcuffs?

US budget deficits have led to a highly leveraged economy, with no immediate solution in sight..

Federal debt is on an unsustainable path

Debt Held by the Public (% of GDP)



Source: Congressional Budget Office

Note: Data includes the long-term projections and other previous projections.

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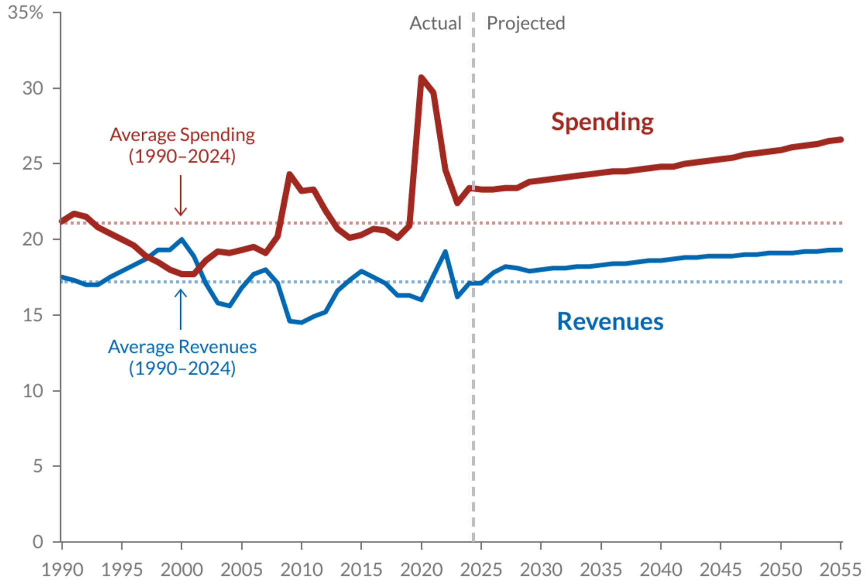
The growing debt is caused by a structural mismatch between spending and revenues

Federal Spending and Revenues (% of GDP)



Source: Congressional Budget Office

Note: Projected data have been adjusted to remove the effects of timing shifts. Data includes the long-term and ten-year projections.

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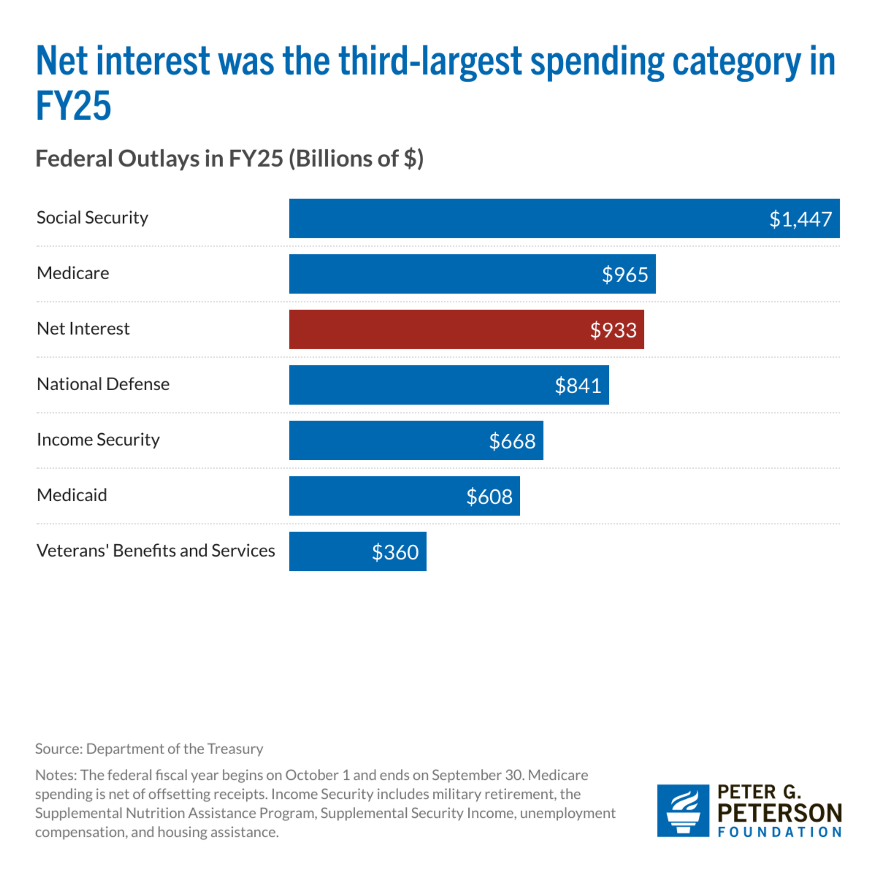
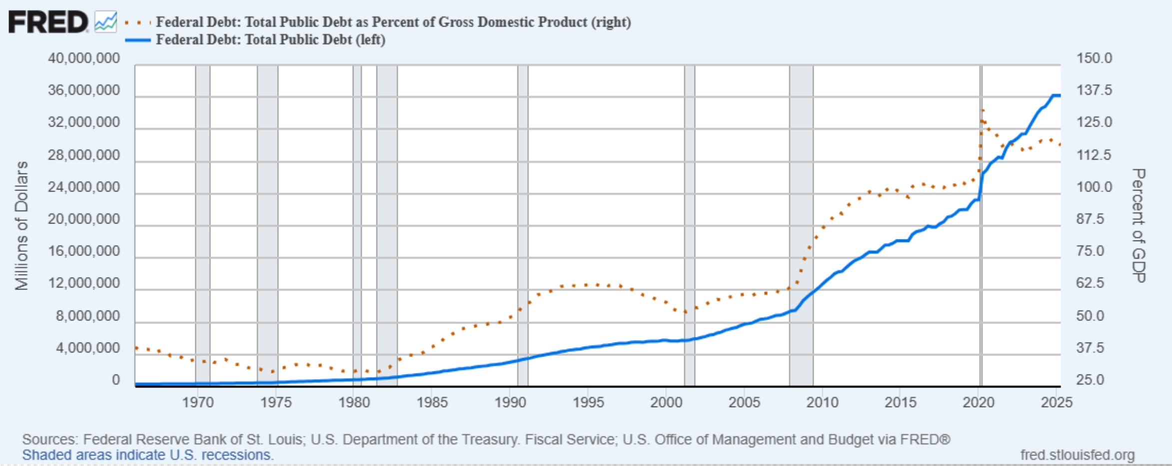
Interest costs have exceeded national defence spending..



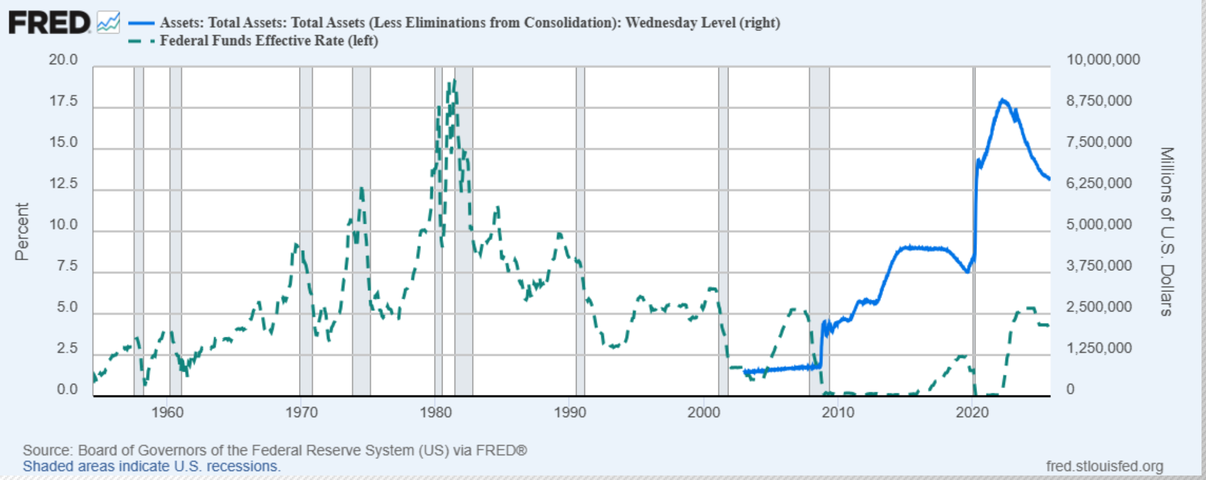


US federal debt has exceeded $38t in October 2025, compared to $37t in August 2025, fastest $1t addition ever. Higher interest costs and ballooning social security costs (due to ageing population) will crowd out other critical spends, including defence.

Does the US Fed have enough fire power to mitigate impact of any sharp decline in US equity markets?

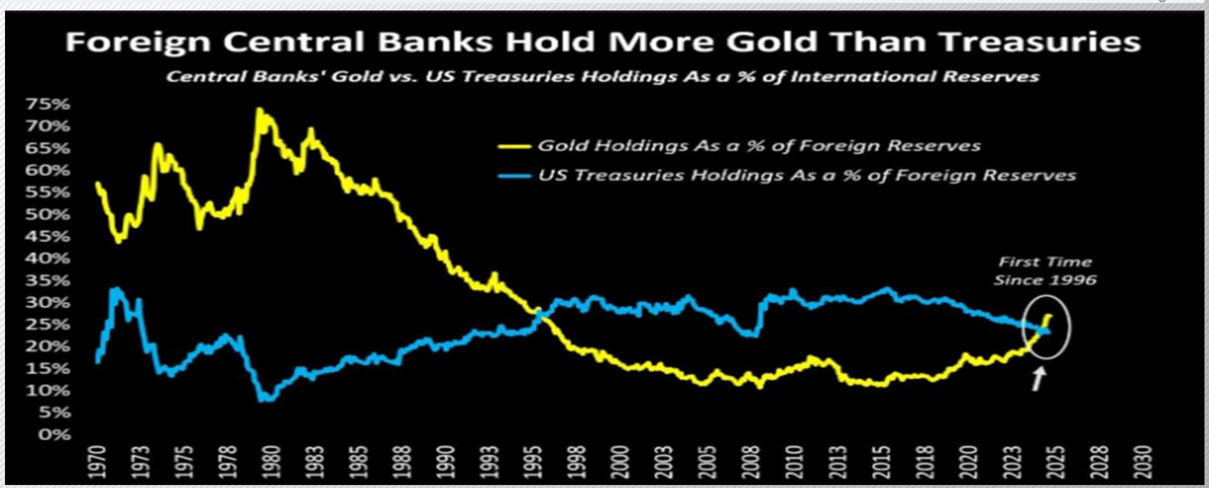
Fed balance sheet has expanded more than 6x in last 25 years.

Fed funds effective interest rate is on a declining trend already, with 50 bps reduction in recent two FOMC meetings.



While US$ continues to be the reserve currency for trade settlement, it has been losing its share as a reserve asset. Gold recently pipped US treasuries as the largest share in foreign central bank reserves. Any new debt issuances by US Treasury that meet with cold water, will create havoc in global financial markets.

"Despite well-founded expectations that American... policy would bolster the Dollar; it has instead fallen... this does reflect growing unease among foreign investors about the currency's trajectory."
-Gita Gopinath



Will the US equity markets crash and cause a global contagion?

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- Are US equity markets overvalued and priced for perfection? Are the US and global ETFs inadequately diversified? Is Rest of the World deeply invested in US equity markets?
  - The answer to all these questions is an overwhelming yes.

- Can a correction be deep like the dot-com bubble in 1999-2000?
  - Difficult to say, but not difficult to visualise. A bad quarter of results from few of the Mag Seven, an AI related surprise from China, rejection of Trump tariff policies by SCOTUS, failures / bankruptcies in private markets, slow down in US economy, flare up in Russia – Ukraine war or a combination of any of these could lead to investors panicking and causing a sell off.

- Can the sell off happen over next 12 months?
  - Once again difficult to answer. Many market experts like Paul Tudor Jones, Ray Dalio, Jamie Dimon and many others, are cautioning investors to stay close to the door or diversify carefully. The sage of Omaha, has been a net seller of stocks for 12 consecutive quarters, accumulating $382bn in cash, a record.