

VALUATION • MARKET HISTORY

# The CAPE Ratio

What 150 Years of Market History Is Telling Investors Right Now

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## Key Takeaways

- The CAPE ratio (cyclically adjusted price-to-earnings, developed by Nobel laureate Robert Shiller) divides price by ten years of inflation-adjusted earnings, smoothing out the noise of any single year.
- The long-run average CAPE is roughly 16 to 17. As of early 2026 it sits near 36 to 38, more than double the historical norm and a level reached only around 1929 and 2000.
- A high CAPE is not a sell signal and not a market-timing tool. It is a statement about the long-run return you are likely buying from today's starting point.
- Historically, when the CAPE has been this elevated, the following decade has tended to deliver below-average real returns. That is a record of what happened, not a forecast.

## Why This Matters

Most investors have no idea their portfolio sits against a valuation backdrop that has appeared only a couple of times in 150 years of market history: once before the Great Depression, once before the dot-com crash. The number that measures it is the CAPE ratio, and right now it is flashing again. This paper explains what it is, what history says about starting from valuations like today's, and the common mistake investors make when they see a high reading.

## The Problem With the Ordinary P/E Ratio

The standard price-to-earnings ratio takes a price and divides it by the last year of earnings. A P/E of 20 means you are paying \$20 for each \$1 of profit. The trouble is that earnings are noisy and swing hard with the economy. In a boom, profits surge and the P/E can look reasonable. In a recession, earnings collapse, the P/E spikes, and the market can look expensive even if prices have fallen.

It is like judging a restaurant by walking past on one slow Tuesday afternoon. A single snapshot does not tell the real story. That short-term distortion is exactly what Robert Shiller set out to fix.

## Enter Shiller and the CAPE Ratio

Robert Shiller, a Yale economist who won the Nobel Prize in Economics in 2013, developed a smarter version of the P/E ratio with his colleague John Campbell. Instead of one year of earnings, the CAPE divides price by the average of the past ten years of earnings, adjusted for inflation. Ten years captures a full economic cycle, booms and busts alike, producing a more stable picture of what the market actually earns over time. They called it the Cyclically Adjusted Price-to-Earnings ratio, CAPE for short, sometimes the Shiller P/E.

Think of it like evaluating a salesperson on their full track record across good years and bad, rather than their last three months. You want the whole picture. That is what CAPE does for corporate earnings.

## What History Tells Us

Since the late 1800s, the long-run average CAPE for the U.S. market has been roughly 16 to 17. Markets near that level are generally fairly valued relative to their earnings history. The chart of CAPE over 150 years has two unmistakable spikes: 1929, just before the crash that began the Great Depression, and around 2000, when it hit 44 at the dot-com peak, the highest reading on record.

Look at what followed each elevated period. Every time the CAPE ran far above its historical average, the years ahead were painful for buy-and-hold investors. Plot CAPE against the returns that followed over the next ten years and the pattern is clear: the higher the starting CAPE, the lower the subsequent returns. It is not perfect, nothing in markets is, but the direction is consistent across 150 years of evidence. This is not a forecast. It is a record of what actually happened.

## Where We Stand Today

As of early 2026, Shiller's data shows a CAPE near 36 to 38 depending on methodology, more than double the long-run average and the second time in the entire 150-year history that it has reached these levels. The first was the dot-com peak in 2000.

There are thoughtful arguments that the CAPE is less meaningful today, that modern technology companies are more profitable and dominant than the industrial firms of a century ago, and that accounting changes complicate direct comparisons. These are not unreasonable points, and today's mega-cap companies genuinely are different animals. But every generation of investors has had its own version of "this time is different," and that phrase has a brutal track record. The math of high starting valuations is stubborn: when you pay a lot for every dollar of earnings, future returns have to work harder to justify the price.

## What Most Investors Get Backwards

Most investors look at a high CAPE and ask, "Should I sell?" That is the wrong question. The CAPE has never been a reliable sell signal. It was elevated for most of the late 1990s, and investors who bailed in 1996 because valuations looked stretched missed three more years of gains before the bubble broke.

The right question is: "What return am I actually buying here?" A high CAPE tells you that your expected long-run return from this starting point is lower than it would be at average valuations. Not zero, not necessarily negative, just lower. And that matters enormously in retirement. If you retire with a million dollars and the next decade delivers 2% annually instead of the 8% to 10% your plan assumed, that gap can be the difference between a portfolio that lasts and one that does not.

*A portfolio built on the assumption that the last decade simply repeats itself, at a CAPE near its historical extremes, is a portfolio built on hope rather than math.*

## What This Suggests, Practically

Given where the number sits, two responses are worth considering with an advisor. First, look harder at diversification beyond U.S. large-cap stocks, which are what is expensive. Many international markets, emerging markets, and small-cap value segments trade at CAPE ratios that are a fraction of the U.S. reading. Diversifying globally is not retreating to safety; it is buying better odds. Second, stress-test return assumptions honestly. A plan built on realistic numbers navigates volatility far better than one built on optimism.

## The Bottom Line

The CAPE ratio will not tell you what the market does next week or next year. Nothing does that honestly. What it offers is a long-run read on the odds, and right now, by this measure, the odds are less favorable than they have been for most of recorded market history. That is not a reason to panic; markets can stay expensive longer than anyone expects. It is a reason to be honest about what you are paying and what you are realistically likely to get in return. Pay attention to price, because over the long run, price shapes your return.

## References and Sources

The following sources support the figures, rules, and statements described in this paper. They are provided for verification and for compliance review.

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