The Possibility Of The Emergence Of Securities Bubbles And Preventive Measures

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Abstract. Securities market bubbles have always appeared week after week in history, and this paper analyzes the inevitability of the emergence of securities bubbles through various arguments. It also suggests methods for ordinary investors to avoid being caught in investment bubbles, as well as demands for curbing securities bubbles from the macro-environmental level.

1.Introduction

In the seventeenth century, the tulip mania swept the Netherlands, with the nobility and servants joining the frenzy, pushing the price of tulips to a new high. And then at a certain point the price collapsed, wiping out thousands of people and plunging the country's economy into chaos, becoming a historical curiosity in economic history.

In today's securities market, if such a bubble occurs, not only the interests of investors are infringed, investment enthusiasm and confidence are drastically hit, the entire securities market will also be impact. If the securities market bubbles bursts, not only the overall business environment is damaged, the reliability of the work of the financial holding will also be threatened [1]. So does a financial bubble as harmful as this still happen in today's securities market? And how do we guard against getting caught in securities bubbles?

2.Main Body

Securities bubbles in the narrow sense is defined as the excess of the price of a security over its intrinsic value, it is the very embodiment of market inefficiency [2]. If we call the part that deviates from the value of a financial asset a bubble, then these bubbles can be said to be ubiquitous in the securities market. Even though the asset pricing theory keeps developing, both the traditional dividend discount model and discounted cash flow model, as well as the modern asset portfolio theory, capital asset pricing model and pricing theory based on behavioral finance, are unable to predict the fluctuation of securities market with 100% accuracy under the uncontrollable behavior of investors, and all of them have the problems of ignoring certain relevant factors, limiting the assumption premise, difficulty in determining the correlation coefficient, so the intrinsic value of stocks cannot be fully determined. Therefore, such a bubble is unavoidable and reasonable in the securities market.

Therefore, the bubbles we are talking about here is more of a miniature of the tulip bubble in the securities market, the price of a security deviates significantly from its intrinsic value and is subsequently inflated until one day the bubbles bursts and the price plummets, hitting investors hard and adversely affecting the securities market as well. Can this happen? The answer is also yes.

2.1 The limited rationality of investors

We cannot simply attribute the emergence of bubbles to the irrationality of investors. We all know that markets are efficient only when rational investors are in the majority, so were the investors in the Tulip Mania irrational? First of all, at that time, the early tulip traders who could think of leveraged trading and trading options were the rational and extremely intelligent part of the market. And then the majority of investors in the market, in the environment of the tulip surge, rather than think that they had lost their ability to objectively judge the value and followed the wind to make the crazy speculation, it is better to think that they were confident that they will be able to sell tulips at a higher price in the future, so that this bubble was getting bigger and bigger. It is undeniable that there are still some noise traders in the securities market, but these noise traders are not the main force of the securities market, and only enough volume to support the rise and fall of securities prices, so the dominant securities market is still those rational investors. But the dominance of these rational investors does not prevent the emergence of bubbles, and in an environment of big rallies, even rational investors inevitably have over-expectations for big hot securities. Securities bubbles usually appear for some surprisingly rational reason, in a predictable way, and then inevitably end in an "irrational exuberance" [3]. The difference is

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that today's securities market has a higher threshold and a more robust regulatory system, unlike the tulips that could be traded even in taverns. On the one hand, it screened out most of the malicious speculators, on the other hand, it made the securities market transactions more standardized and risk more controllable.

2.2 The emergence of "potential" things

In the final analysis, bubbles are created by people's confidence that the price of the asset will continue to rise or rise rapidly in the short term. So as long as the times are constantly developing, people will continue to have confidence in new things. In the early 21st century, with the rise of the Internet, almost everyone was optimistic about the development of the Internet, and investors invested a lot of money into Internet companies, imagining that they could make a good profit from the development of this new industry. The U.S. government failed to do a good job of top-level planning and timely guidance, allowing social venture capital to over-hype the Internet office, Internet business and other new industrial sectors, and directly leading to the early 21st century Internet bubble [4]. But most Internet companies could hardly escape the fate of recession after the boom, the Internet bubble burst. So that countless investors lost a lot in this investment, and the entire Internet industry has caused a serious blow. So when a new industry or innovative technology emerges, it will undoubtedly inspire investor's confidence in the industry and cause a wave of investment, but when the wave is too high, it is still unclear whether the industry into which the wave is coming will be able to withstand the excessive expectations of investors. Sometimes it is not even the emergence of a new industry that drives the influx of investors to that industry, but simply the momentary frenzy of people for some traditional industries can do so. When people's enthusiasm and expectations flood into these industries, it drives up the price of securities, and if the companies that bear the expectations are not capable enough to keep up with the soaring prices, then the bubbles can easily burst.

2.3 The interest behind the bubbles

One is the benefit that investors expect to gain, and the other is the benefit that malicious manipulators really gain. Investors caught in the bubbles believed that if they bought the asset at the current price, as long as the asset continued to appreciate, and based on the speed of bubbles expansion at that time, they could benefit from the huge price difference. The lure of such benefits and the investors' own self-confidence made them have a wrong perception of risk. For example, the interest of the companies in creating the capital market "bubble" in order to further manipulate profits [5]. And those behind the manipulation of the capital side, as long as the early entry, laying traps to lure a large number of investors into the bureau, and when the bubble blows up and investors get into a frenzy ,they leave, then they can extract benefits from investors, and let the ordinary fanatical investors to bear the consequences of the bubble bursting. After the banker's goods are distributed, no one to maintain the price of securities, there is no reason not to fall, thus forming the bursting process of the securities market bubbles, and the majority of individual investors trapped in the trap set for the "herd" [6]. People's tendency to profit, as well as overconfidence make them neglect and misjudge the risk, involuntarily step into the bubbles. The huge profits that can be obtained by the controllers behind the bubbles, will also attract them to violate the morality and create the bubbles.

The bubbles in the securities market expands quickly and bursts even faster, so you can imagine that once you are caught in such a bubble, most investors will find it difficult to pull out. So how do we prevent the securities bubbles, avoid the risk of falling into the securities bubbles and incurring huge losses due to the bubbles bursting, and promote the healthy development of the securities market?

1. Indexing investment

"An indexed investment strategy is the one I most recommend for investors to adopt. At a minimum, the core portion of every portfolio should be indexed." The author of A Random Walk Down Wall Street mentions passive indexed fund investing several times in his book. With consistent indexing over time, investors should be able to avoid huge losses caused by bubbles and even achieve more desirable returns. For most investors who want to save time and effort, choosing indexing is arguably one of the best options. Choosing indexing allows us to discard most of the outside influences, such as the emotional investment brought by company stories and the influence of untrue outside information on investment decisions. Use real numbers to illustrate the problem, and use data to keep investors rational.The more indexed investors, the more passive stock holders than active stock holders, which makes the private information content of the stock price less [7]. More importantly, just like "Don't put your eggs in one basket." the portfolio chosen for indexing can also diversify the investment risk, and reduce the investor's losses in case of a stock bubble.

2. Establish a sound early warning mechanism

Generally speaking, the emergence of bubbles in the securities market is characterized by symptoms. For example, abnormal capital flow into the stock market; when hot money, led by capital management funds, floods into the securities market, it often leads to asset prices within the market that do not match the real value, increasing the securities market bubble [8], soaring P/E ratios and intensive investor investment intentions may lead to securities bubbles. By monitoring the movement of these data at all times and detecting the signs of bubbles in time, we can more effectively promote the risk avoidance of the emergence of securities bubbles. The emergence of a bubble requires the support of a large number of investors, so it is important to keep an eye on some speculative news, and find out whether there are capitalists maliciously behind the investigation to encourage people to invest, blow up the bubble. Such behavior is very bad, because a large number of investors

are attracted to enter the carnival, and continue to push up the price of securities, and once the bubble burst, the most serious losses are also these ordinary investors. Therefore, the establishment and improvement of early warning device to help identify the bubbles in advance, and the kill of bubbles in cradle, can effectively prevent investors from falling into the bubble, the maximum extent of timely stop loss.

3. Enhance the supervision of the securities market

The SEC is the maintainer of order in the securities market, and the regulator should to reduce the creation of bubbles, control the continued growth of these bubbles and try to recover the losses caused by the bubbles bursting, it plays a crucial role in the risk avoidance of bubbles. The financial regulatory system is mainly set up to avoid financial risks, and its important role is to avoid financial risks [9]. One of the major reasons for the emergence of the stock and securities bubbles is the inadequate regulation of the financial market, the stocks value cannot reflect the real operation of the real economy, resulting in serious problems [10]. Therefore, the SEC should actively perform its duties of supervision and management. Firstly, it should ensure the public disclosure of market information to help investors make investment decisions with more adequate information. Secondly, when there is a hint of abnormal rise or fall in the price of a security, promptly investigate and collect evidence on that security. And when find malicious manipulation of the securities market and other illegal acts, impose severe punishment according to relevant regulations. Finally, the relevant department should listen to and deal with the reasonable demands of investors, and clarify the arrangement of investor compensation mechanism to further protect the legitimate rights and interests of investors.

4. National policy adjustment

Generally speaking, there are two types of policies for state intervention in the securities market: monetary policy and fiscal policy. Both policies do not prevent human beings from falling into bubbles by suppressing their nature, but can channel investors' enthusiasm into safer areas. Monetary policy, with its quick results and immediate impact, is an aggressive approach. While fiscal policy, with its slow results and sustained impact, is more moderate than monetary policy. Because of the low interest rates on savings and the minimal returns on even the safest government bonds, many people choose to put their money into the riskier corners of the market in exchange for higher returns. It follows that if the country implements a corresponding monetary policy to raise the interest rates on both, then investors will be less enthusiastic in the securities market. However, this method, for one thing, has a wider degree of influence and cannot precisely combat the enthusiasm of investors caught in the bubbles, and when investors have fallen into the bubble mania, it has little effect, for another, the subsequent adjustment is difficult. The Tulip Mania at the time lasted only 6 months before bursting, and in today's information-driven world, this time will be significantly reduced. But this does not mean that fiscal policy, which can only work for a long time, does not work for the bubbles in the stock market. Tax policy, for example, will also have an impact on the securities market. Generally speaking, lower tax rates can reduce the burden of enterprises to increase efficiency, and also allow investors to increase their income and stimulate investment, thus stimulating the rise of securities prices. The government's issuance of treasury bonds will also have an impact on the securities market, thus leading to a corresponding fall in securities prices. Of course, it is not wise to overly suppress the enthusiasm of investors in the investment market. The best way is for the state's intervention policy to indirectly regulate the securities market, using the policy to help build a balanced and stable securities market environment, which can more effectively help investors avoid the risk of securities bubbles.

3.Conclusions

The emergence of bubbles in the securities market is inseparable from human nature. Although the emergence of bubbles is caused by various reasons, human nature can be said to be a necessary condition for the emergence of bubbles. Therefore, although securities bubbles do not occur all the time, they do not stop appearing either. From the Tulip Mania, the 1929 U.S. stock market crash, the Japanese stock market and real estate market madness, to the biotech companies boom in the 1980s and the dot-com boom in the 1990s. These financial bubbles always go round and begin again, but no matter how many lessons have been learned before, people always get caught in bubbles again and again. In today's securities market is no exception, such bubbles are still possible and will burst in shorter and shorter time, the limited rationality of investors will make them fall into the bubble, and the confidence of investors will make them too late to pull out and take the knocks of bubbles bursting. These securities bubbles will undoubtedly disrupt the securities market, hurt ordinary investors, discourage investors from investing and make them lose confidence in the securities market. In order to effectively prevent the occurrence of securities bubbles and reduce their impact, not only are investors asked to sharpen their vigilance to identify bubbles and choose some wiser investment methods. But more effective measures are to control the occurrence of bubbles from the perspective of the overall macro policy and market environment, be alert to the emergence of bubbles, and take measures to reduce investors' losses and the impact of bubbles on the market after the appearance of them, effectively avoid the risk of bubbles and create a safer investment environment.

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