

Using Past Market Bubbles to Predict the Next One

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Over the last 25 years, the U.S. stock market has twice hit historically high valuations, followed by deep and lasting bear markets. Today we're once again closing in on historic highs: The S&P 500 Index, a good proxy for the U.S. stock market, closed at a record high of 6144 on February 19, 2025.

So, it's understandable that many investors are worried about whether we might be in the middle of yet another bubble in the stock market. A recent report highlighted by Newsweek noted that nearly **26%** of Americans expressed worry that Wall Street might hit rock bottom, implying a significant level of concern among the general retail investor population.

What will happen to *your* investment portfolio if it turns out that we are in a bubble, and the bubble bursts? History provides some clues. During the last two stock market bubbles (2000 and 2008), many investors lost *half of their life savings*. And after a market bubble bursts, it takes a long time to recoup those losses. It took almost five years to recover from the 2008 crash. And if your grandparents were in the market in 1929, it took them *25 years* to finally get all their money back.

Are we in a bubble today?

The short answer is yes. (See chart below) But the longer answer is a little more complicated. Just because the market is in a bubble doesn't mean that it's going to burst anytime soon. Bubbles can, and often do, continue to grow bigger and bigger over time.

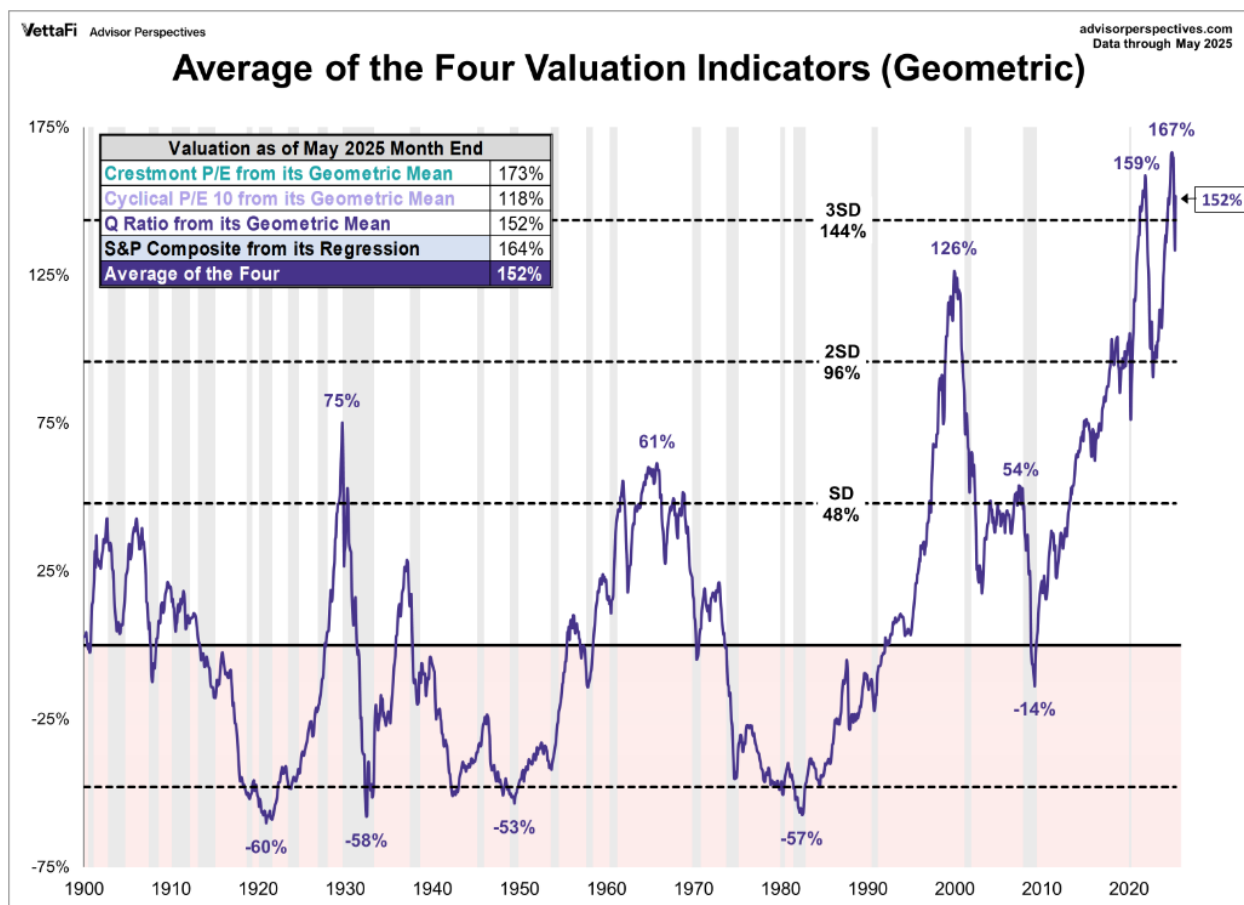
For a bubble to burst, it must expand well beyond its previous high-water mark. Sometimes, these new record highs are justified. Most measures of valuation say that the market today is somewhere between moderately expensive and very expensive.

But bubbles are different. In a bubble, investors go crazy and bid up the price of the asset in question to absurd levels of overvaluation. It's this manic speculative behavior that's the key to identifying a bubble.

In this paper we will take a look at some of the most notorious bubbles in history, so that we can recognize the warning signs and avoid the next one. Because there will ALWAYS be a next one.

First, let's take a look at where we are today on the bubble scale. Using four separate measures of market valuation, the chart below shows that the market is 152% above its fair value. Fair value for our purposes is the average of four valuation indicators used by Jennifer Nash at Advisor Perspectives.

How overvalued is this market? More overvalued than it was at past bubble peaks in 1929, 2000, and 2008. I think it's fair to say that we are in a valuation bubble, but history tells us that big bubbles can continue to inflate for a long time, until some catalyst (like a recession) comes along and pops it.



Even though our current bubble is not ready to burst yet, there are a few warning signs out there. One is the record amount of borrowing that's taking place at retail brokerage firms like Schwab and Fidelity. When people borrow money for investing in the market, it can be an indication of overconfidence and excessive risk-taking on the part of unsophisticated (retail) investors.

Another sign of market stress is the recent surge in daily volatility. The last few years have been relatively calm and quiet in the market, but starting in January 2025, the market has seen big daily moves – both up and down – and it looks like the trend will continue for a while.

The best way to avoid taking a major hit to your life savings when the next bubble bursts is to look at what happened during past bubbles and ask:

- What caused them?
- How much damage did they do?
- What were the warning signs?
- What can this bubble teach us?

Defining terms and parameters

A **bubble** is a sharp and prolonged rise in the market price of an asset. The asset can be anything that's traded in a public market. Gold, houses, stocks, bitcoins, and even tulip bulbs (yes, tulip bulbs!) are all examples of assets that have experienced speculative price bubbles in the past.

These asset bubbles are caused by an out-of-control stampede of demand by investors. When investors pour so much money into an asset that they drive the price beyond any rational measure of its fundamental value, the result is a bubble.

Since prices are no longer connected to fundamental value, they eventually pop. And when they do, the money that was invested in them simply vanishes – often overnight.

A **crash** is a sudden and violent drop in the value of a market, often caused by the popping of a bubble. When an asset bubble bursts, too many investors try to get out of the market at the same time. Attempting to avoid more losses, investors during a crash begin to panic, and as a result will sell their holdings to anyone who will buy them – regardless of how low the price is. This panic selling contributes to the snowball effect of declining prices. The relationship between bubbles and crashes is strong. Historically, bursting bubbles almost always end with market crashes. But all market crashes are not necessarily caused by asset bubbles. More on that later.

It is important to note the distinction between a crash, a bear market, and a correction. While crashes and bear markets are sudden and violent, a correction is usually shorter, shallower, and less damaging for investors.

A **correction** is the market's way of dampening the enthusiasm of investors who may be getting a little carried away. As a rule, corrections are declines of between 10% and 15% in the market.

The reason for wanting to predict the next bubble is to avoid the pain that happens after it pops. Understanding the difference between an upcoming crash and a simple correction will help you make better decisions that will ultimately protect your life savings.

Anatomy of a Bubble

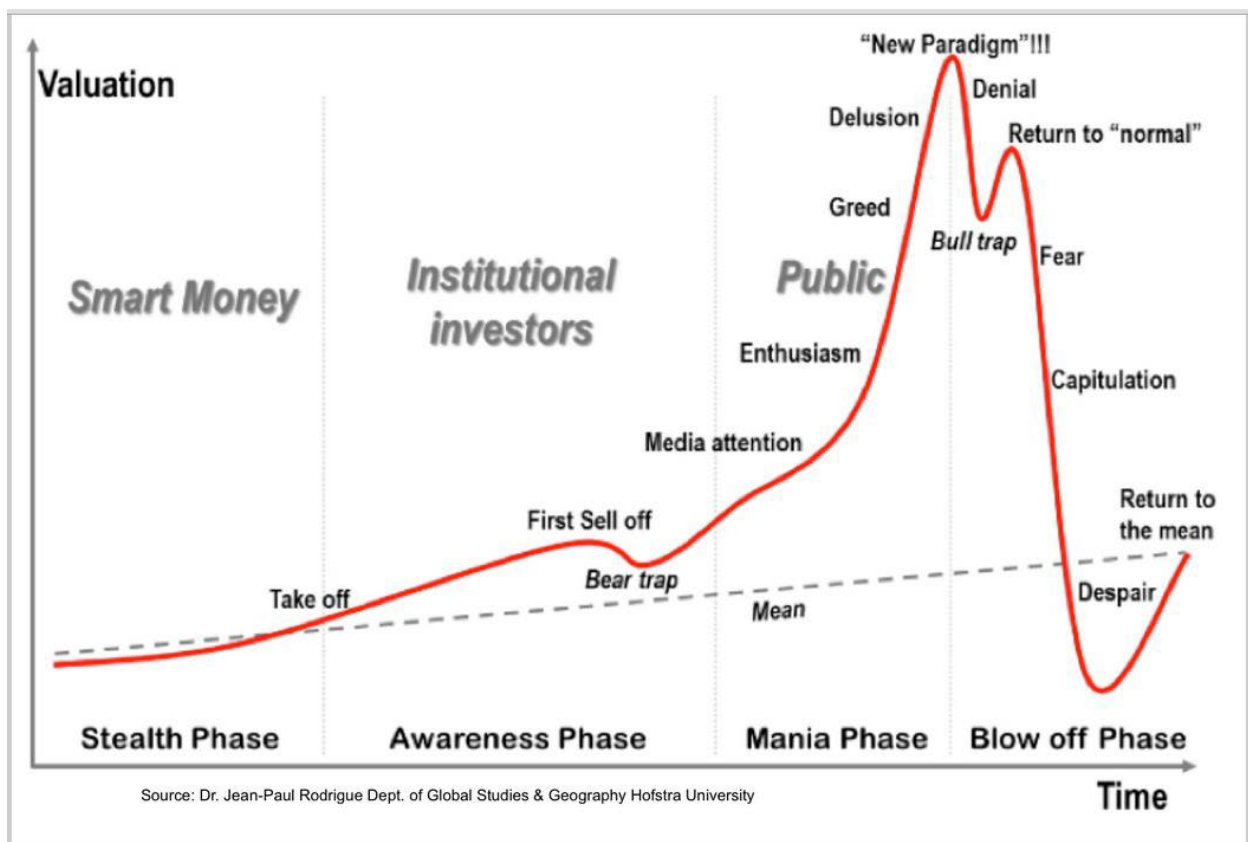
The chart below shows the phases of a typical market bubble. During the “stealth” phase, the so-called “smart money” quietly accumulates bigger and bigger positions in the market. Who is the smart money? Professionals like hedge funds, bank traders, corporate insiders, and global asset managers.

They’re considered smart because they have access to the best information, they have close relationships with the movers and shakers inside the companies they invest in, and they have very deep pockets, which allows them to write big commission checks to the Wall Street firms who show their appreciation by keeping these investors informed about what’s coming next.

When the smart money spots the potential for an asset to take off, they begin to quietly accumulate a large position. Once they are on board, the stealth phase ends and the awareness phase begins.

During the awareness phase, the smart money strategically leaks information about their positions to big institutional investors (like mutual funds and pension plans), who then start to get on board. The third phase is the beginning of the mania. This is when the “dumb money” finally notices the rising prices and decides to get on board.

Who is the dumb money? The relatively underinformed retail investors. In other words, almost everybody else. There are about 100 million retail investors out there, and unless you’re very wealthy or extremely well-connected, you’re probably part of the dumb money. This doesn’t mean that you’re dumb. It just means that you don’t have enough money in your brokerage account to attract the best and brightest minds in the investment advice world.



The fourth and final phase is the blow-off period, where the trend is so obvious that it becomes mainstream news, and everybody wants to get in on the action. You can tell that you're in the blow-off phase when the market becomes a popular topic of conversation at parties.

Importantly, during the final stages of the bubble, the early investors (smart money) are the ones who are selling to the latecomers. Once the speculative boom runs out of buyers, the party is over. Wave after wave of selling by the big institutions continues to hammer the price of the asset until the only ones left holding the bag are the mom and pop retail investors.

Note the changing emotions among investors as the bubble progresses through the four stages. Bubbles create emotional extremes, and fear of being left behind is what drives the final blow off stage of the bubble.

Also note that markets never move in a straight line. There are always some zigs and zags along the way. These little bumps in the road often cause what market technicians call "bear traps" and "bull traps." A bear trap is a temporary dip in the market that fools some investors into believing that the rally is over. They get spooked and sell out prematurely, only to watch helplessly as the bull market starts up again. A bull trap is the opposite. Here the bubble has already burst, but there is a sudden and sharp bounce that fools some investors into believing that there is more room to run on the upside. They buy into this mini rally, only to watch the market turn around and continue its sharp decline.

One of the keys to recognizing that we might be in a bubble is the phenomenon known to market historians as the **New Paradigm**. This is a widespread belief, perpetuated by the media, that "things are different this time." What that means is that it has become clear that the market is overvalued, so the way to justify this is to throw out the old measurements of valuation and bring in new ones. This is the new paradigm.

Beware of any talk of a new paradigm when the market is making new highs, as it is today. When you begin to read and hear experts using phrases like "the old rules don't apply" or "this is the new normal" or "valuations don't matter as much

today” it’s a big red flag. It doesn’t mean that you should sell everything right away, but it does mean that you should keep one eye on the exit at all times.

Now let’s look at some of the most infamous bubbles of all time.

- [Tulip mania](#) (1637)
- [South Sea](#) (1720)
- [The Great Crash](#) (1929)
- [Silver](#) (1980)
- [Japan](#) (1989)
- [DotCom](#) (2000)
- [U.S. Housing](#) (2007)

When does an overpriced asset become a Bubble?

An asset bubble can be evaluated using these three metrics:

1. **Price:** The magnitude of the price increase of the underlying asset
2. **Impact:** The total size of the market for the asset
3. **Recovery Time:** How long it took for the asset to reach its prior high after bursting

I use these three metrics because they are useful for eliminating bubbles that are too small to have a significant impact on the investing community at large. There are dozens, if not hundreds of asset bubbles that lack the size and scope that is required to make it onto the list of the greatest bubbles of all time. The greatest bubbles will score highly on all three metrics. They will be a large market with extreme price changes that takes several years to recover after bursting, if ever.

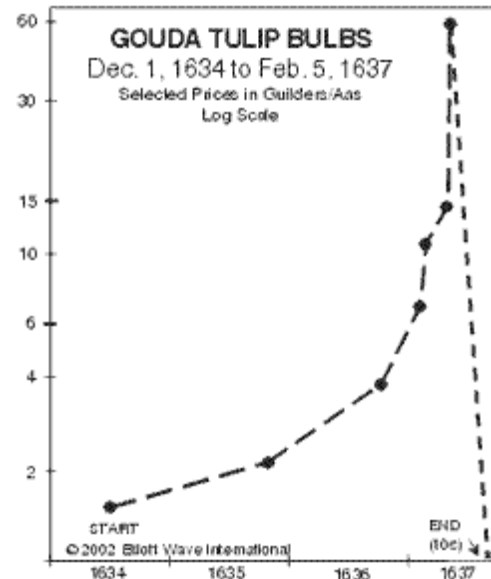
[Dutch Tulip Mania \(1636-1637\)](#)

The first time I heard about the tulip bubble in Holland, I thought it was a made-up story- something you might read in The Onion. But it was real, and it was as serious as a heart attack. Tulips had been a prized possession among the Dutch

ever since they were brought to the Netherlands from the Ottoman Empire in the mid-1500s. The Dutch fell in love with tulips, and this eventually led to one of the greatest asset bubbles of all time.

Generally considered to be the first recorded asset bubble, the Tulip Mania of 1636-1637 was an episode in which tulip bulb prices were bid up by speculators to unimaginable heights before collapsing and dragging the Dutch economy into a deep and prolonged depression.

Tulips only bloom for about one week, with bulbs appearing between June and September. Because of this short window for harvesting and trading bulbs, a rudimentary tulip bulb futures market arose so that growers and traders could speculate in tulips all year round.



What Caused It?

Tulip prices steadily rose with their growing popularity and bulbs were purchased at higher and higher prices by speculators who planned to turn around and sell them for a profit, similar to modern-day "house flippers."

From 1634 to 1637, an index of Dutch tulip prices (see chart) went from about one guilder per bulb to a frothy sixty guilders per bulb. Traders who sold their bulbs for a profit then reinvested all of that profit into new tulip bulb contracts. People would sell everything they owned in order to get enough cash to purchase a few tulip bulbs. They were convinced that they would be able to sell them for more profit than they could have ever made in a lifetime of working. By the peak of tulip mania in February of 1637, a single tulip bulb was worth about ten times a craftsman's annual income.

Successful Dutch tulip bulb traders, an early version of the day traders of the dot.com bubble and the house flippers of the U.S. housing bubble, could earn up to 60,000 florins in a month (approximately \$58,600 in current U.S. dollars.) Tulip

bulb speculation became so widespread in 1636 that they were eventually listed for trading on Amsterdam's Stock Exchange.

The Crash

Like all bubbles, the Dutch tulip bulb bubble continued to inflate beyond anyone's wildest expectations until it abruptly "popped" in the winter of 1637. A default on a tulip bulb contract was the main catalyst and caused the market to violently implode. Sellers overwhelmed the market and buyers virtually disappeared overnight.

Some of the bigger traders tried to support prices, but to no avail. Within just a few days, tulip bulbs were worth only a small fraction of their former prices, resulting in a full-blown panic throughout Holland. Dealers refused to honor contracts, further damaging confidence in the market.

When the Dutch government tried to stem the tulip market meltdown by offering to honor contracts at 10% of their face value, it only caused more panic and heavier selling. The bursting of the tulip bulb bubble ended the Dutch Golden Age. It would take a generation for Dutch investors to recover from the crash of the tulip bulb market.

Takeaways

What can we learn from Tulip Mania? For one thing, it should be obvious that paying ten times your annual salary for a single tulip bulb was crazy. And yet people did exactly that. How is this possible? The answer lies in one of the strongest motivators in the world of investing – the fear of being left behind.

We saw this in 2000, when dot.com stocks were trading at prices that were so ridiculous that the analysts had to make up new ways to value these companies. That was a tulip-like warning.

The other takeaway is that when you see people who you know to be cautious and conservative but are suddenly talking enthusiastically about how much money they're going to make in the market, that's a big red flag. No matter how big the rally in the market, stick with your long term investing strategy. Don't step outside of your normal level of risk taking. It will almost always end badly.

The South Sea Bubble (1720)

In the 1700s, the British Empire was the dominant player in global finance. For the British, the eighteenth century was a time of prosperity and opulence. There was a large portion of the population who had money to burn and were looking for opportunities to diversify their land holdings. So, the South Sea Company (hereafter SSC) came along to fill that need. It attracted thousands of eager investors when it secured the "rights" to all trade in the South Seas.

What Caused It?

The first issue of stock in the SSC didn't satisfy the appetite of the first group of speculators. After they were assured of the company's future success, they demanded even more shares. The story being sold was that Mexicans and South Americans were eager for someone to sell them wool and fleece in exchange for jewels and gold. The story was so compelling, and the demand for shares so strong, that the SSC kept issuing more and more shares to the public. People bought the additional shares as fast as they were printed.

But behind the scenes there was trouble. The people who ran the company were inexperienced business managers. But they were experts at marketing, so they set up fancy offices and furnished them with elegance and opulence. People, once they saw the wealth the SSC was creating, couldn't buy shares fast enough.

Britons were eager to invest their money. They were blind to the fact that the SSC was poorly managed

and losing money quickly. The British people kept buying, because they saw their neighbors getting rich and they didn't want to be left behind. The SSC, and others like it, gave the British people what they wanted. The demand for more opportunities created an IPO frenzy that included offerings of stock from companies that promised to reclaim sunshine from vegetables and to build floating mansions to extend Britain's landmass. They all sold like hotcakes.

The Crash

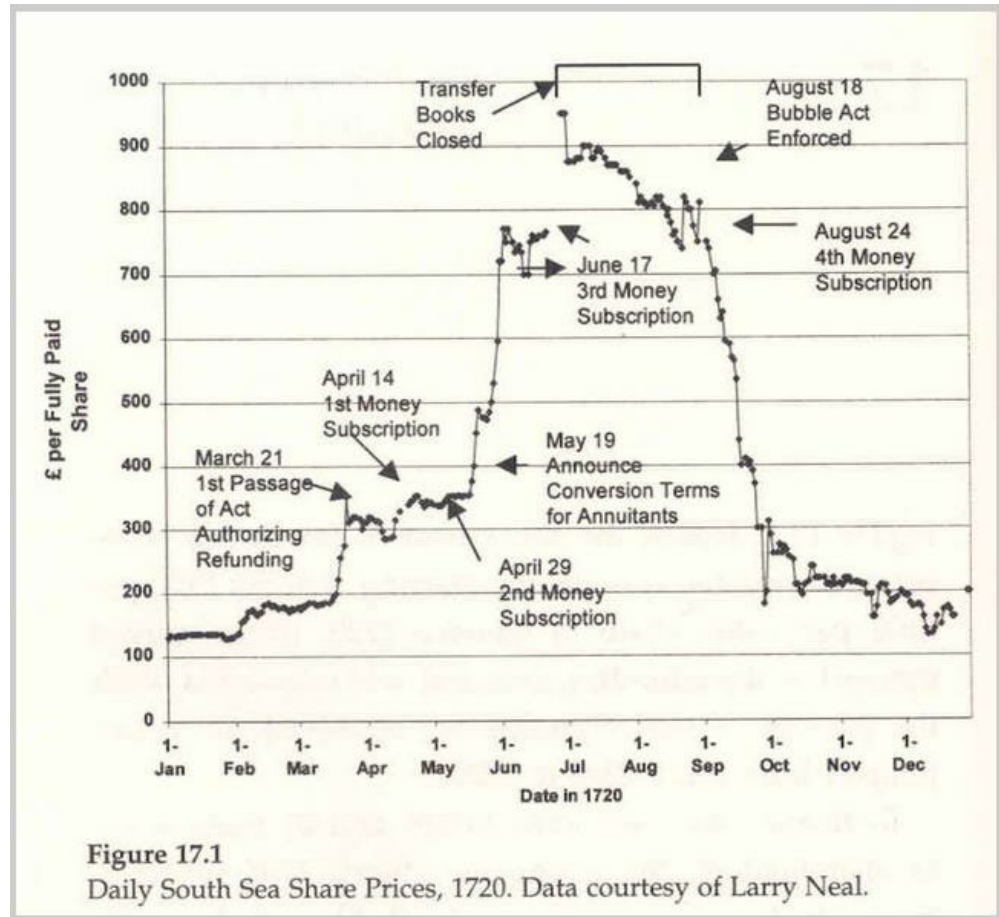
Eventually the management team of SSC realized that the value of their shares in no way reflected the actual value of the company or its dismal earnings. So, they sold their stocks in the summer of 1720 and hoped no one would leak the

failure of the company to the other shareholders. Eventually word leaked about company insiders selling, and panic ensued. The huge hole in the south sea bubble dragged many of the other high-flying IPOs down with it. It was the end of the golden age of stock market speculation in Britain.

Takeaways

In many ways, the South Sea bubble was similar to tulip mania. The warning signs were everywhere, if you were paying attention. But there's an important difference here. In the case of tulips, everyone knew what they were, and how they worked. Dig a hole, stick the bulb in the ground, and you get a nice flower. No mystery.

But with the South Sea bubble, there was no way to know what you were getting. This is the classic pig in a poke problem. So my takeaway here is to never, ever invest in any company or any asset that you can't understand, and especially if the person who is trying to sell it to you can't explain it.



Now let's move on to another historically significant market bubble.

The Crash of 1929

From its' peak in September 1929, to the bottom in July 1932, the U.S. stock market lost nearly 90% of its value. The economic and social fallout from the bursting of this massive bubble was enormous. It sent the country into a depression that lasted throughout the 1930s. What caused the crash? Could it happen again? What can an investor do to avoid getting caught up in a crash as bad as this one?

What Caused It? In the fall of 1929, America was partying like crazy. It was the Roaring Twenties, and the stock market was rocketing higher and higher, setting new records nearly every day. Everybody was getting in on the action, and many were borrowing money so they could buy as much stock as possible. The stock market was sure to make everyone rich.

Since the stock market had been going up for years, it was believed to be a no-risk bet, and many people poured their life savings into it. With this flood of new and unsophisticated investors, the market was ripe for manipulation. Investment bankers, brokers, traders banded together to form "pools" whose sole purpose was to manipulate stock prices and get out with gains.

They did this by subtly acquiring large chunks of stock between them and trading them between each other for slightly more each time. When the public noticed the progression of price on the ticker tape, everyone would buy the stock. The market manipulators would then sell their overpriced shares for a healthy profit. On and on the cycle went as these unscrupulous investors turned a profit by selling their manipulated, over-priced shares to unsuspecting amateurs who desperately wanted to get in on the action.

The Crash

Eventually, everyone who wanted to get into the market was fully invested. Demand flattened out, and there were no more buyers around to keep prices going up. When the big banks and brokerage firms saw what was happening, they began to cash out. As prices began to fall, a panic ensued. By the time the dust settled, the market had fallen almost 90%.

What happened next is one of the darkest chapters in American history. Banks began to fail as the public lost confidence in them. Unemployment spiked to nearly 25%. The Great Depression was in full swing.

The Great Depression had an impact on other countries too. Stock markets around the world crashed. A banking collapse took place in the United States. Extensive new tariffs and other factors contributed to an extremely deep depression. The United States did remain in a depression until World War II.

Takeaways

There were several causes for the 1929 crash and the Great Depression. Massive speculation, market manipulation by inside operators, massive borrowing by the public to fund more stock purchases, and a loss of confidence in the banking system. The market today is more structured and regulated than it was back then, but there is no guarantee that a 1929 style crash can't happen again.

One of the unique features of this bubble was the ability to buy stock with a 5% down payment. This meant that you could buy \$1,000 worth of stock by putting up \$50 and the broker would lend you \$950. As long as the market continued to go up, you would make a killing. But when the market stumbled, the broker would demand repayment. If you couldn't come up with the money, the broker would sell your stock. This massive, forced selling is what caused the crash of 1929.

Recent bubbles

You might think that people would learn from the painful lessons of history, and that bubbles would eventually disappear from the investing landscape. But unfortunately, that's not the case. Bubbles are about psychology and emotion. They are driven by greed, and perpetuated by gurus, pundits, and the mass media, who stand to benefit from selling books and attracting viewers. As long as capital markets exist, there will be bubbles.

The dot.com bubble of 1997-2000, and the housing bubble of 2003-2007 are the most recent examples of markets behaving badly. Other bubbles include things like gold, bitcoins, and social media stocks.

The Dot.com Bubble (2000)

When the dot.com bubble burst in 2000, the stock market went into a two year slide that didn't stop until it had lost 78% of its value. This marked the end of the first internet boom. A brief look at the history of the internet will shed some light on how the dot.com bubble came to pass.

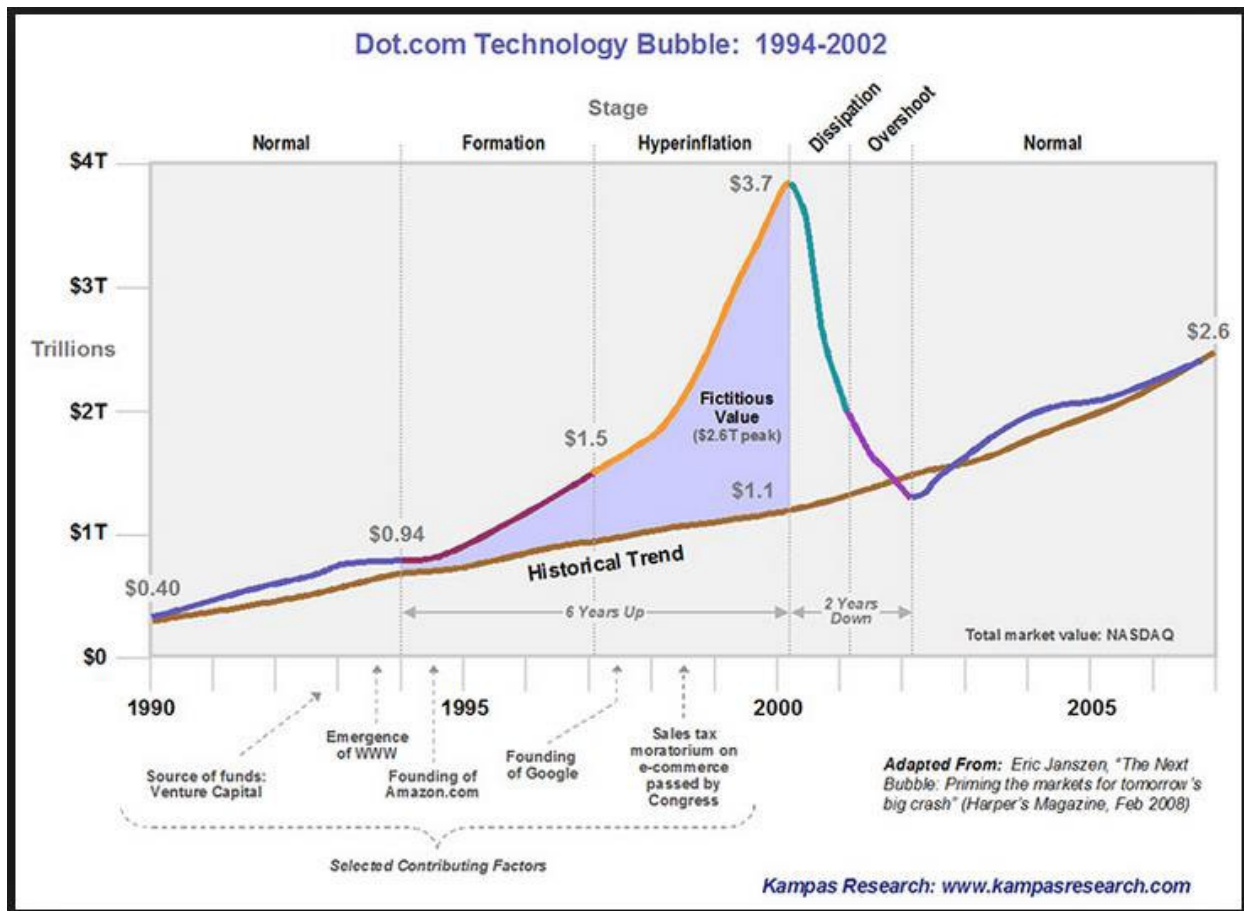
Invented by U.S. military engineers in the 1960's, the internet as we know it didn't really take off commercially until 1995. At that time there were an estimated 18 million internet users. Silicon Valley entrepreneurs began to notice that there was an untapped market there - an international market. So, they started to create businesses to take advantage of this potential.

Stock market investors were barely able to control their excitement. There was widespread talk in the media of the arrival of a "new economy." (Sound familiar?)

As the internet boom really started to take off, the new tech companies began to realize that investors wanted big ideas more than big profits. Buzzwords like networking, chat rooms, consumer-driven navigation, tailored web experience, and other examples of techno-babble filled the media and created a stampede of investors who wanted to get in on the ground floor of the internet revolution.

The IPOs of internet companies accelerated in frequency and size, sweeping the nation up in euphoria. Investors were blindly grabbing every new issue without even looking at a business plan to find out, for example, how long the company would take before making a profit, if ever.

(See chart next page)



The Crash

Obviously, there was a problem. The first warning signs for this bubble came from the companies themselves. Some reported loss after loss, with the losses getting bigger with each announcement. Some ran out of money and declared bankruptcy within months of their initial offering.

Then came the revelation that the game was rigged. It turns out that there was an unholy alliance between the investment bankers and the startup companies. Here's how it worked. The investment bank would drum up interest in the startup company by taking the management team on a tour across the country (called a "road show"), telling potential investors that it was bound to become the next Microsoft, Apple, or IBM.

In exchange for this glowing praise, the startup agreed to pay the investment banker handsomely. Payment was in the form of underwriting fees for the IPO.

The problem was that many of these startups didn't have a prayer of making any money – and the bankers knew it. But it didn't matter, because the appetite for internet IPOs was immense, and the bankers knew they would hit pay dirt no matter what happened.

The Takeaway

Many argue that the dot.com boom and bust was a case of too much growth happening too fast for young entrepreneurs to manage it properly. Companies that couldn't even articulate their mission were given millions of dollars with hardly any strings attached. Anyone who was paying attention to fundamental measures like sales or earnings could see that things were getting a little crazy.

Today we're seeing a similar bubble developing in social media stocks, which I think are the dot.com stocks of today. (More on the social media bubble later.)

Here's my advice. There are some great companies out there, and they will undoubtedly make lots of money over many years. But how can you know which ones will succeed and which will fail spectacularly? The answer, if you're being honest with yourself, is that you don't.

So be careful about how much you pay for these companies. Don't buy them the first day they come out. Don't buy them if they don't have any earnings. And don't commit more than 5% of your capital to the social media industry as a whole.

Next let's take a look at the housing and credit bubble that took place between 2003 and 2007, which led us to the financial meltdown of 2008 and the Great Recession.

The Housing Bubble (2003-2007)

The S&P 500 fell 57% from its high in October 2007 to its low in March 2009. Following the bursting of the dot.com bubble and the recession of the early 2000s, the Federal Reserve kept short-term interest rates low for an extended

period of time. This coincided with a global savings glut, as developing countries and commodity-producing countries accumulated large pools of cash.

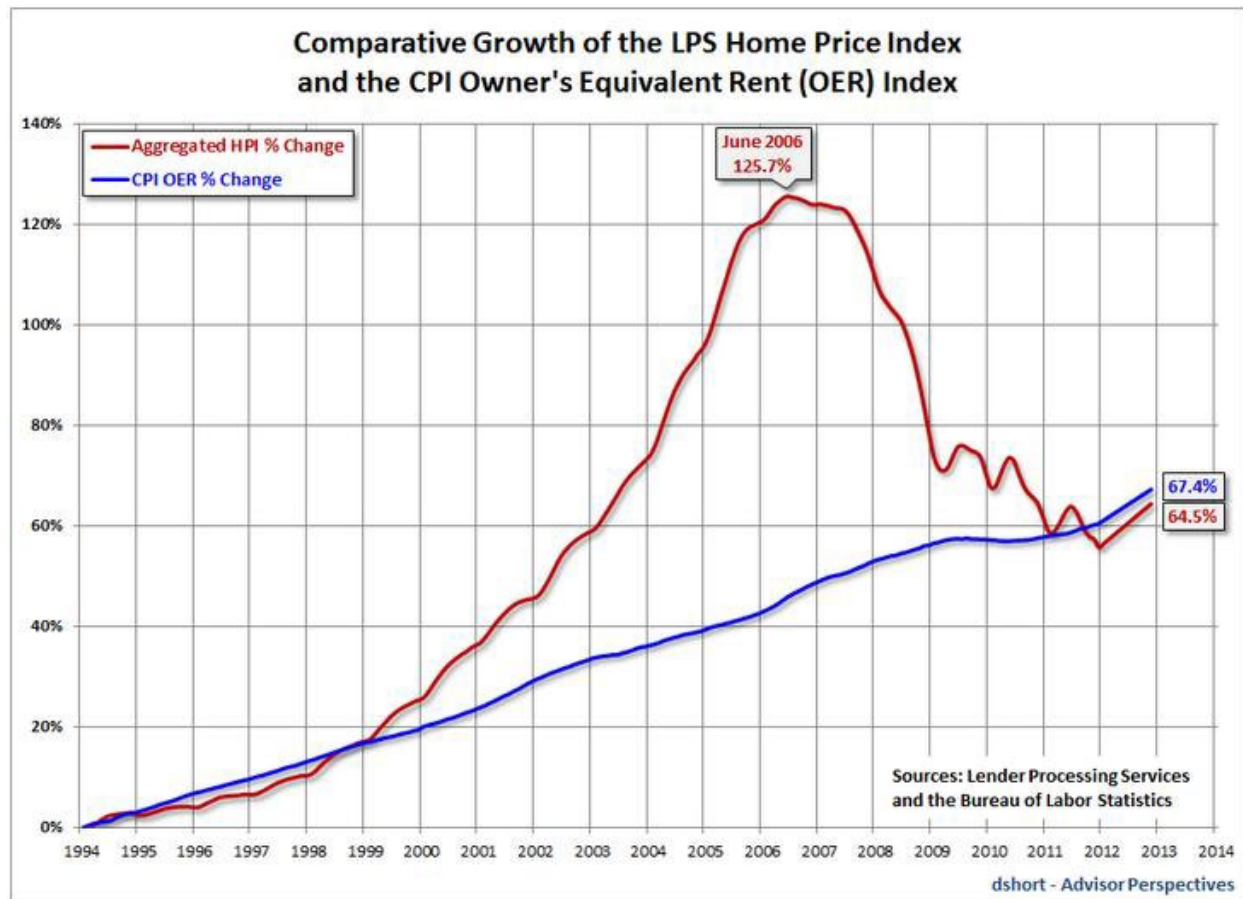
As these excess savings were invested, global interest rates declined to record low levels. Frustrated with low returns, investors began to seek out higher returns wherever they could find them.

What Caused It?

In the United States, home prices took off (particularly on the two coasts and in cities such as Phoenix and Las Vegas.) Rising home prices led to rampant real estate speculation, and also fueled excessive consumer spending as people began to view their homes as an ATM that they could extract cash from to finance expensive purchases.

As home prices continued to soar and many homeowners "stretched" to make their mortgage payments, the possibility of a collapse grew. However, the true extent of the danger was hidden because so many mortgages had been sliced, diced, packaged, and sold to investors who were looking for an alternative to government bonds. This created tremendous demand for mortgage lending, which

in turn created a situation where anyone who could fog a mirror could get a mortgage – often with no proof of employment or income.



The Crash

When the long held belief that home prices would always go up turned out to be false, prices on these packaged mortgage products plunged, creating big losses for banks and mortgage brokers. These losses soon spread to other financial markets, fueling a crisis of confidence in the health of many of the world's largest banks. Events reached their climax with the bankruptcy of Lehman Brothers in September 2008, which resulted in a credit freeze that brought the global financial system to the brink of complete collapse.

Unprecedented government intervention helped to temporarily ease some of the panic in the marketplace, but by late fall in 2008, widespread rumors surfaced that Lehman Brothers was about to collapse. Rumors began to circulate that Citigroup, Bank of America, and other large banks would have to be nationalized if the global financial system was to survive. Fortunately, the coordinated rescue by governments around the world prevented a total financial collapse.

It took until March of 2009 for the stock markets around the world to stabilize, and for the panic over the possibility of total global financial collapse to fade into the background.

The Takeaway

Over the last 15 years, investors have experienced bubbles and market crashes with ever-increasing frequency. I think it's important for investors to remember that the circumstances that will create the next crisis will probably be very different from the circumstances that created the last crisis. What I mean by that is, while excessive greed in the financial markets is an unavoidable human tendency, so too is excessive fear. Investors who can incorporate the lessons of the credit crisis without having their emotions unduly influenced will be better prepared to weather the next storm when it arrives.

Silver (1980)

In 1980 the Hunt brothers tried to corner the silver market. They created a buying panic and forced the short sellers to cover their positions. They drove the silver price to \$48.70/oz before margin calls forced them to begin liquidating their positions.

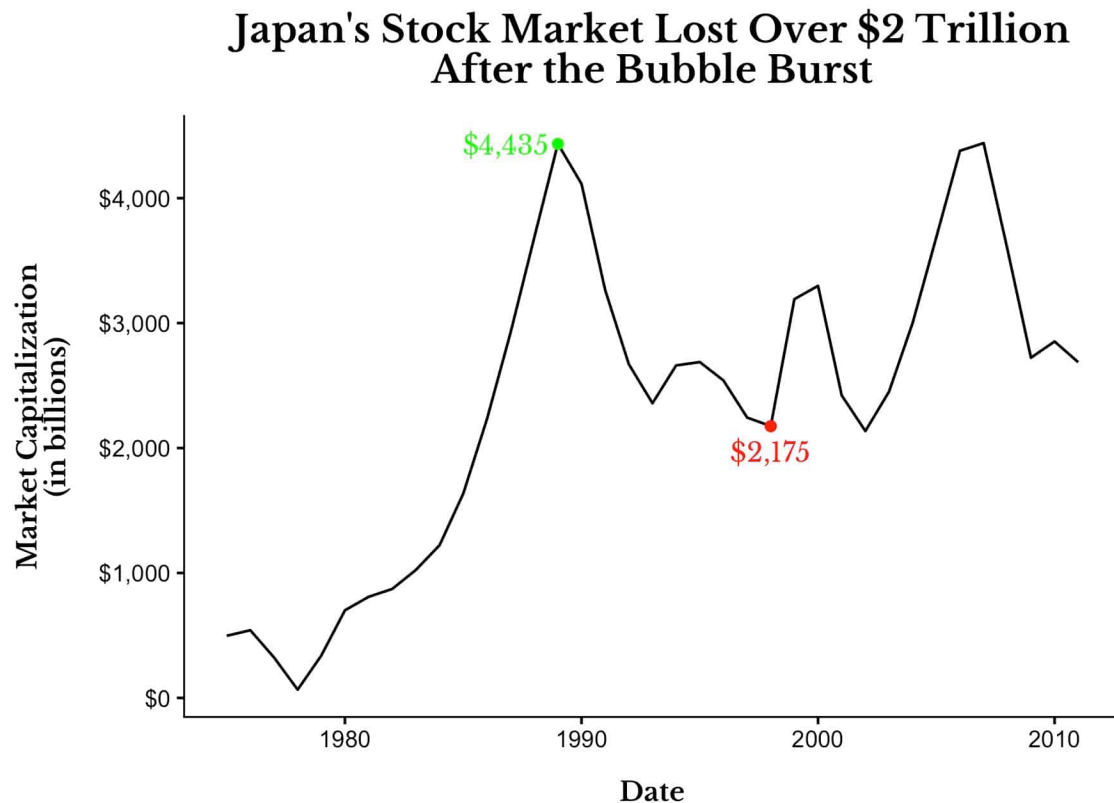
Silver crashed from \$48.70 to \$10.96, wiping out the two brothers and earning an honorable mention in the history of great speculative asset bubbles. While this bubble scored high on price movement and recovery time (silver today is trading at \$23/oz), it scored low on market capitalization relative to other bubbles, so would likely not be considered the greatest ever. The entire market value for physical silver today is about \$1.3 trillion – less than half as much as Apple Inc.'s \$2.9 trillion.

Japan (1989)

Japan in the late 1980s was riding high. At the peak, the Japanese imperial palace was considered to be worth more than [all the real estate in California](#) and the

Japanese stock market had grown 10x over the prior decade. More importantly, in the 33 years since the peak, both Japanese stocks and residential real estate have yet to recover.

To be precise, the Japanese stock market lost over \$2 trillion and Japanese land values have declined by \$8 trillion since the late 1980s/early 1990s. (See below charts.)



Source: FRED (OfDollarsAndData.com)
Note: Japan's market capitalization is listed in 2011 dollars.

Final Observations

Bubbles are inherent in any capital market mechanism. Except for rare cases (like the Hunt brothers attempt to corner the silver market in 1980) bubbles are not created by dark forces deliberately trying to manipulate prices to their own advantage. What they really are reflects human emotion. When investors see a big move in the market, and especially when they hear stories of others making a

killing from the move, it can be nearly impossible to resist the temptation to join the party.

It's usually the small, retail investors who create most of the risk in the marketplace by inflating stock prices beyond the value of the underlying company. When stocks are flying through the stratosphere like rockets, it is usually a sign of a bubble. That's not to say that stocks cannot legitimately enjoy a huge leap in value, but this leap should be justified by the prospects of the underlying companies, not just by a mass of investors following each other. The unreasonable belief in the possibility of getting rich quick is the primary reason people get burned by market crashes. Remember that if you put your money into investments that have a high potential for returns, you must also be willing to bear a high chance of losing it all.

Another observation we should make is that regardless of our measures to correct the problems, the time between crashes has decreased. We had centuries between fiascos, then decades, then years. We cannot say whether this foretells anything dire for the future, but the best thing you can do is keep yourself educated, informed, and well-practiced in doing research.

So, what can an investor do to avoid getting caught up in a modern day version of Tulip Mania? The best way to protect yourself from another crash is to diversify, avoid buying on margin, and stay away from stocks that are extremely overpriced. Investors forgot these commonsense safeguards in 2000, when

they fell all over each other to buy technology stocks that were trading at massively inflated prices. The dot.com bubble, and the 2008 housing bubble are the closest we have come to a repeat of the 1929 market crash and Great Depression. In short:

- Don't invest in anything that you don't understand.
- Don't invest in something just because everyone else is.
- If you must speculate, never risk more than 5% of your capital on any one bet.

Before you climb on board the next bubble, consider how you might react if you were the last one on board before the bubble popped.

Coming Up Next

It's one thing to read about market bubbles, but it's another to apply the type of critical thinking that's really required to monitor your own portfolio.

In my next newsletter, I'll be going into more detail about how to stay on top of your investments, make changes at the right time, and ultimately avoid the crashes. And if you avoid the next crash, you will be in a much better position to take advantage of cheaper prices. If you haven't signed up for my (free) newsletter, you can do so here: www.zeninvestor.org

Here's a list of sources I used while researching this paper, along with links to relevant pages.

David Leonhardt, New York Times columnist

http://www.nytimes.com/2014/05/06/upshot/time-to-worry-about-stock-market-bubbles.html?_r=0&abt=0002&abg=1

Jesse Columbo, economic analyst, and Forbes columnist

<http://www.thebubblebubble.com/historic-crashes/>

FINVIZ.com, a website that offers data visualization tools

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