**Behavioral Finance Explains Stock Market Bubble**

**We are "Human", not "Rational"**

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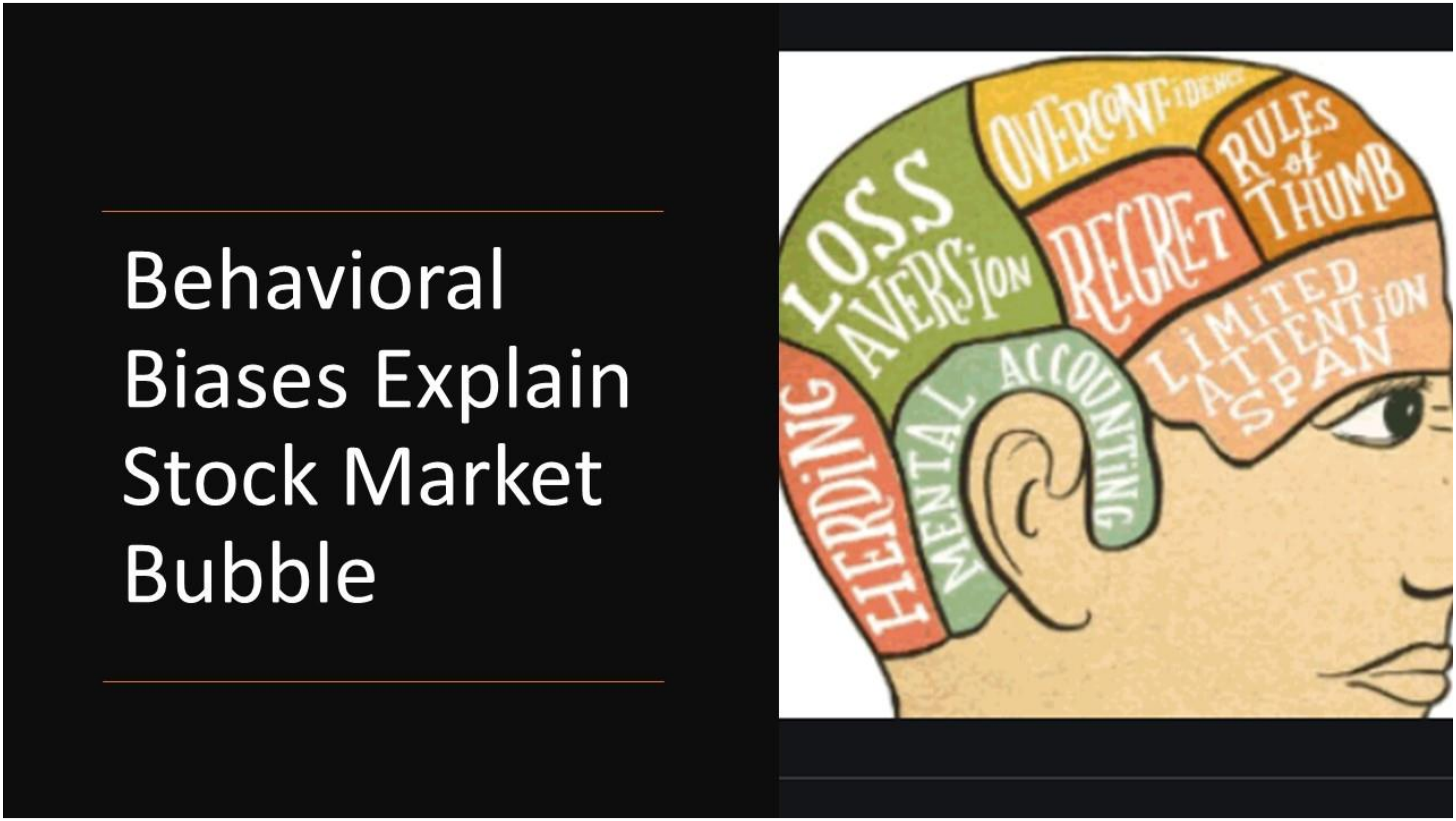

Who isn't baffled by the continuing run-up in stock prices? Behavioral scientists. They explain that we all have a host of biases that make us irrational. Here are the reasons that we have a stock market bubble, presented in 2 tables.

| Bubble Inflators | Behavioral Bias |
|---|---|
| 1 Vaccines will cure the pandemic quickly | Base rate fallacy |
| 2 Earnings will soar in an economic recovery | Gambler's fallacy |
| 3 Federal Reserve will dump $trillions | Hyperbolic discounting |
| 4 Interest rates will remain low | Recency illusion |
| 5 Greed:  FOMO is fear of missing out | Dread aversion |
| 6 Investor euphoria: Hopium | Irrational escalation |
| 7 Huge foreign demand | Confirmation bias |
| 8 Millennials believe markets only go up | Continued influence effect |
| 9 FAANG Stock phenomenon | Less-is-better effect |
| 10 Apple &Tesla are each worth a fortune | Neglect of probability |
| 11 The election. | Normalcy bias |
| 12 Belief that amateurs can beat Wall Street | Overconfidence effect |
| 13 Stock buybacks | Outcome bias |
| 14 SPACs: Special Purpose Acquisition Companies | Pro-innovation bias |
| 15 IPOs: Initial Public Offerings | Decoy effect |
| 16 Inflation caused by money printing is ignored | Money illusion |

Biases: Source Wikipedia

| Bias | Type | Description |
|---|---|---|
| 1 Base rate fallacy | Extension neglect | The tendency to ignore general information and focus on information only pertaining to the specific case, even when the general information is more important |
| 2 Gambler's fallacy | Logical fallacy | The tendency to think that future probabilities are altered by past events, when in reality they are unchanged or actually worse |
| 3 Hyperbolic discounting | Extension neglect | The tendency for people to have a stronger preference for more immediate payoffs relative to later consequences |
| 4 Recency illusion | | Favors recent events over historic ones |
| 5 Dread aversion | Prospect theory | Just as losses yield double the emotional impact of gains, dread yields double the emotional impact of savoring |
| 6 Irrational escalation | Logical fallacy | People justify increased investment in a decision, based on the cumulative prior investment, despite new evidence suggesting that the decision was probably wrong. |
| 7 Confirmation bias | Confirmation bias | The tendency to search for, interpret, focus on and remember information in a way that confirms one's preconceptions |
| 8 Continued influence effect | Confirmation bias | The tendency to believe previously learned misinformation even after it has been corrected |
| 9 Less-is-better effect | Extension neglect | The tendency to prefer a smaller set to a larger set judged separately, but not jointly. |
| 10 Neglect of probability | Extension neglect | The tendency to completely disregard probability when making a decision under uncertainty. |
| 11 Normalcy bias | Cognitive dissonance | The refusal to plan for, or react to, a disaster which has never happened before. |
| 12 Overconfidence | Egocentric bias | Excessive confidence in one's own abilities |
| 13 Outcome bias | | The tendency to judge a decision by its eventual outcome instead of based on the quality of the decision at the time it was made. |
| 14 Pro-innovation bias | | The tendency to have an excessive optimism towards an invention or innovation's usefulness throughout society, while often failing to identify its limitations and weaknesses |
| 15 Decoy effect | Framing effect | Preferences for either option A or B change in favor of option B when option C is presented. |
| 16 Money illusion | | The tendency to concentrate on the nominal value (face value) of money rather than its value in terms of purchasing power |

## Conclusion

Rather than trying to make logical sense out of the bubble, we need to accept that it is not logical. Sometimes the easiest explanations are the best.