

Speculation and market bubbles

Speculation and market bubbles: it is one of market failures. Price cannot reflect the true value of assets when there is speculation.

How market bubble arise?

When speculators expect that the price of the stock of the company will rise over time

- ↳ They buy the stock of the company.
- ↳ Demand for a stock rises.
- ↳ Price of stock of the company also increases.
- ↳ When price of the stock rises, it creates incentive to buy more to get capital gain.
- ↳ One day when the company cannot make profit as much as people expected.
- ↳ People sell off a lot of the stock.
- ↳ Price of stock falls dramatically.
- ↳ "Bubble burst"

