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Irrational Exuberance

NEW YORK TIMES BESTSELLER
IRRATIONAL EXUBERANCE
REVISED AND EXPANDED THIRD EDITION
ROBERT J. SHILLER
WINNER OF THE NOBEL PRIZE

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Synopsis

In this revised, updated, and expanded edition of his New York Times bestseller, Nobel Prize-winning economist Robert Shiller, who warned of both the tech and housing bubbles, cautions that signs of irrational exuberance among investors have only increased since the 2008-9 financial crisis. With high stock and bond prices and the rising cost of housing, the post-subprime boom may well turn out to be another illustration of Shiller's influential argument that psychologically driven volatility is an inherent characteristic of all asset markets. In other words, Irrational Exuberance is as relevant as ever. Previous editions covered the stock and housing markets and famously predicted their crashes. This edition expands its coverage to include the bond market, so that the book now addresses all of the major investment markets. It also includes updated data throughout, as well as Shiller's 2013 Nobel Prize lecture, which places the book in broader context. In addition to diagnosing the causes of asset bubbles, Irrational Exuberance recommends urgent policy changes to lessen their likelihood and severity and suggests ways that individuals can decrease their risk before the next bubble bursts. No one whose future depends on a retirement account, a house, or other investments can afford not to read this book.

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This first edition of this book, in 2000, was a broad study, drawing on a wide range of published research and historical evidence, of the enormous stock market boom that started around 1982 and picked up incredible speed after 1995. The book argued that the boom represented a speculative bubble, not grounded in sensible economic fundamentals. The second edition, in 2005, added an analysis of the real estate bubble as similar to the stock market bubble that preceded it, and warned that "Significant further rises in these markets could lead, eventually, to even more significant declines." Alas, both predictions turned out to be true, as we now all know. Will history repeat itself with this third volume? That is hard to say. In this latest edition, Professor Shiller updates his argument, and augments the text to reflect developments since the 2005 second edition. Of particular interest, he adds an important new chapter on the bond market, which many feel is also in bubble territory. The good news is that, while Professor Shiller says that returns in all asset classes are likely to be subpar for some years given today's elevated asset prices, the mood is less somber than in previous editions, and there are no warnings of imminent doom, as in previous editions. In particular, he does not see a classic "bubble" in bonds, due to the lack of "exuberance" -- prices for bonds are being bid up reluctantly by investors, he says, which is not the formula for a bubble. However, he certainly balances that somewhat comforting news with a realistic view of the risks that the current situation presents to investors and savers of all types, stocks, bonds, housing, and savings accounts.

This reviewer remembers having read the first edition of this book back when it first came out in either 1999 or 2000, just before the stock market crash of 2000-2001. It did a very good job at providing historical perspective regarding long-term values in the stock market. It, correctly, pointed out that the stock market was overpriced and that a decline would be reasonable to expect. And so it happened. Since then, bubbles have also burst in the housing market worldwide as well as the stock markets. In addition, commodity markets have taken on many of the speculative characteristics of equity and housing markets, characteristics that they have not had, at least to the extent of the equity and housing markets, in the past. Bubbles in these markets were not discussed in the first edition of the book. For this reason this reviewer purchased this edition of Dr. Schiller's book - to obtain historical perspective on the housing markets, equity markets since 2000 and commodity prices. The book, in short, provides very good historical perspective on the first two of these (housing and equity markets) but, unfortunately, not too much regarding commodity markets. It discusses long term trends and cyclical bubbles in their historical context. For this reason alone
this book should be read by serious investors and students of both economics and finance. As Aristotle once said "A man with no perspective has no value". In addition to providing historical context in regard to these markets, the book also does an excellent job at explaining, through the lens of economic psychology, why bubbles occur. The primary reason is that there is human interaction, that taken on the aggregate, influences the market as a whole.

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