Some *Facts* About the Tech Bubble in the Late 1990s

(Some of the Slides from a Recent NBER Discussion)

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3. Nasdaq Beta.
The Less Famous NYSE High Tech “Bubble”

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Trading Volume in Tech Stocks

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- Nasdaq Turnover increased somewhat.
  * But it peaked well after the “bubble” burst.
- NYSE Hi Tech Stocks’ Turnover did not move at all
- Nasdaq Hi Tech Stocks’ Turnover went down.
Why Did the “Bubble” Burst?

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- Nasdaq’s Profitability plummeted in 2000.

(Source: Pastor and Veronesi “Was There a Nasdaq Bubble in the Late 1990s?” JFE, 2006)
Was it a Bubble?

- It is possible that prices exceeded fundamentals in the late 1990s for tech stocks.
- However, an explanation based on short sales constraints may find it hard to explain why *exactly* the same pattern of return, volatility and “risk” occurred in NYSE Hi Tech stocks.
  - Short sales constraints are much less binding for NYSE stocks.
- Short sales constraints though may have played a role in Nasdaq
  - The “bubble” was stronger in Nasdaq
  - Trading seemed more active in Nasdaq during the “bubble” period (but it peaked later).
Was it a Bubble?

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(see Pastor and Veronesi “Was there a Nasdaq bubble in the late 1990s?” , 2006, JFE)
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  – This story explains all of the facts discussed earlier.

  1. High uncertainty about long term growth + low risk aversion imply (very) high prices.
  2. High uncertainty implies a high return volatility and a high beta.
  3. High uncertainty implies a strong reaction of prices to bad news in profitability (and hence price drop)
  4. High uncertainty + differences of opinion implies a high trading volume.
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– Moreover, it explains other facts about the late 1990s

1. High uncertainty increases option value of new ventures and thus increase incentive to go public

⇒ IPO wave of tech stocks at the end of the 1990s
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  (See Pastor and Veronesi, “Technological Revolutions and Stock Prices,” NBER WP 2005)
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  - This model implies all of the stylized facts discussed earlier.