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BURSTING THE BUBBLE: SPECULATIVE FERVOR THEN & NOW

Last week marked the anniversary of one of the most famous financial bubbles in history: Tulipmania. Nearly 400 years ago, during the early 1600s in the Netherlands, speculation on tulip bulbs reached extraordinary levels. Prices soared as investors rushed to buy, convinced that the value of tulips would only rise. But as is the case with all bubbles, reality eventually set in. Prices collapsed, fortunes were lost, and the episode became one of the earliest recorded examples of speculative excess.

At its core, Tulipmania wasn't about tulips; it was about human behavior. Investors got caught up in the excitement, fueled by fear of missing out, herd mentality, and irrational expectations. Markets are made up of people, and the fact is that people are not always rational. Behavioral investing studies the ways in which emotions like greed and fear can impact decision-making. Time and time again, history has shown that when speculative fervor takes hold, asset prices can detach from fundamentals and reality, often leading to painful corrections. And while the world has changed dramatically since the 1600s, investor psychology remains remarkably consistent.

What fuels a bubble? First, let's consider herd mentality which is when investors see others making money and rush in, assuming prices will keep rising. Next, overconfidence plays a large role as many find themselves believing "this time is different" and that the laws of supply, demand, and valuation no longer apply. Finally, humans often favor storytelling over substance and justify high prices with exciting narratives rather than solid fundamentals. Eventually, emotional excitement dwindles and reality reasserts itself. When sentiment shifts, the unfortunate outcome is that prices often fall faster than they rise.

While markets have certainly evolved since Tulipmania, the human tendency toward speculative behavior remains unchanged. Today, a handful of large technology companies have driven a disproportionate share of recent market returns. While these companies possess strong business models, we suggest the possibility that their valuations may be stretched, making investors vulnerable if sentiment changes. Also, consider how the past few years have seen explosive rallies in speculative assets like cryptocurrencies and meme stocks, driven by social media enthusiasm rather than underlying business fundamentals. Finally, the excitement surrounding Artificial Intelligence (AI) has propelled some stocks to extraordinary valuations. While AI is undoubtedly transformative, distinguishing real opportunity from investor hype is critical. Currently, capital expenditure budgets are quite high, and this is where our fundamental, bottom-up research process comes into play.

At Crawford, we retain our optimism about the possibilities that come with long-term investment in high-quality stocks. While we are not implying that high prices for stocks today mean that they must endure a period of serious losses, we do suggest the possibility exists that we may experience more pedestrian returns going forward. We believe our disciplined, long-term, quality-oriented investment approach provides an antidote to speculative excess. Rather than chasing what's "hot," we put fundamentals first and focus on companies with strong balance sheets, sustainable earnings, and proven business models.

At Crawford, we use dividends as an indicator of quality along with the aforementioned attributes, believing that a commitment to returning capital to shareholders often reflects financial strength and prudent management. We also believe in the benefits of an appropriate level of diversification and avoid putting too much faith (or capital) into any single asset or trend. Finally, it is an awareness of the impact of human behavior and inefficiencies this creates that is possibly the most important factor in driving long-term success. This avoidance of emotion enables us to resist the temptation to follow the herd and exploit potential behavioral inefficiencies to the benefit of our investors.

The lessons of Tulipmania still apply today: bubbles form when speculation outpaces reality, and they burst when reality catches up. While markets will always experience periods of euphoria and fear, long-term success comes from staying disciplined, avoiding speculative frenzies, and focusing on remaining invested in high-quality investments that can weather the test of time. At Crawford, we believe that investing with prudence, not emotion, is the best way to build and preserve wealth. While speculative excess will always be part of markets, history reminds us that those who stay patient and committed to quality tend to fare best in the long run. We have several conventions built into our investment process to protect against overconfidence and behavioral biases. The quality orientation we seek in our investment portfolios reinforces all this, and we intend to continue to adhere to our long-term discipline.