

Expectationally Driven Market Volatility: An Experimental Study

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We study the existence and robustness of expectationally driven price volatility in experimental overlapping generation economies. In the theoretical model under study there exist “pure sunspot” equilibria which can be “learned” if agents use some adaptive learning rules. Our data show the existence of expectationally driven cycles, but only after subjects have been exposed to a sequence of real shocks and “learned” a real cycle. In this sense, we show evidence of *path-dependent* price volatility.

The existence of multiple equilibria in economic models has been a persistent embarrassment to theorists and a source of controversy in the formulation of macroeconomic policy. In models of dynamic economies, indeterminacies frequently manifest themselves as so-called “sunspot” equilibria. In these equilibria, the expectation that extrinsic random events matter becomes self-fulfilling, and causes extrinsic uncertainty to have real allocative effects.