

RESEARCH

BESS at MNB (MNB-CEU)

Ambiguity, Information Acquisition and Price Swings in Asset Markets

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Venue: MNB-Visitor Centre (1054 Budapest, Szabadsag ter 8.)

Abstract

This paper studies asset markets where Knightian uncertainty about the fundamentals can be mitigated through costly information acquisition. In these markets, investors' information choices can be strategic complements, resulting in multiple equilibria, history-dependent prices, and large price swings occurring after small changes in uncertainty. Our model makes a number of predictions about the market response to uncertainty shocks, including crashes, followed by sustained rallies and price overshoots, and switches in information regimes, which the model generates due to the information complementarities. Our model highlights uncertainty as a new channel for episodes of extreme price volatility and media frenzies.

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