

Information choice and economic complexity

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Research question

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How should you choose what information to analyze when the economy is ex-ante complicated?

Alternatively, how much information is it rational to ignore?

Information choice

Information choice is the study of how investors choose what things they wish to know about.

In asset pricing, we like to think about how information choice impacts things like

- Expected returns
- Risk premia
- Welfare (?)

I use “information choice” and “attention” synonymously.

My hypothesis

I am trying to find out whether “complex” economies cause the basic findings of information choice models to fall apart.

Common findings:

- When a “common component” of payoffs or returns becomes more volatile, more attention goes to the common component. Common component here might be the business cycle or market returns.
- Increased attention reduces excess volatility, while decreased attention increases excess volatility.
- Prices are informative about payoffs because prices are a function of investor attention.

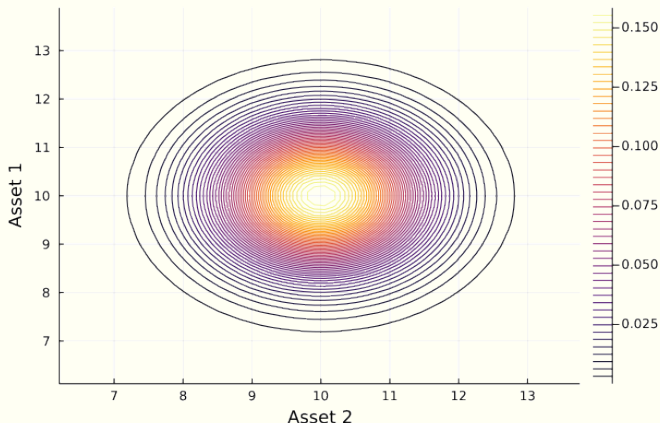
My hypothesis

What I think might happen:

- Investors allocate attention in a way that can systematically mislead them about the state of the economy.
- Attention allocation can increase or decrease excess volatility/returns in a biased way.
- Prices may be **very informative** or **not informative at all**, since investors with different information can interpret prices radically differently.

In short – the **findings of information choice models might not be as clear in complex economies.**

Complexity



Traditional models of information choice use unimodal joint densities with good properties. The above is the case used in Kacperczyk et al. (2016).