"Over- and Under-Confidence in a Correctly Specified Model"

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Abstract

Growing literature concerns a Bayesian rational decision maker who learns the parameters of a data-generating process (DGP) while her behavior influences the DGP. The main focus has been to show how misperception persists when her model of the DGP is misspecified. This project aims to show that misperception may persist even when the model is correctly specified. We focus on one of the main reasons why identification of the true parameters fails in a correctly specified model; as the decision maker learns about the DGP, her behavior provides less and less variation to pin down the true parameters.