Discussion of

The Keynesian Beauty Contest: 
An Economic System, the Mind, and the Brain

Rosemarie Nagel, Felix Mauersberger, Christoph Buehren

by Sascha O. Becker
My own research

- Economic History (Protestant Reformation, WWII etc)
- Education Economics (gender gap in education)
- Political Economy (Brexit)

… i.e. **not** a macro-economist
Discussion of

The Keynesian Beauty Contest:
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Overview of developments

- A truly superb HB chapter on the developments in experimental economics
- ... and of Keynesian BCs
- ... and of behavioral Regularities in BC-Experiments and Level-k.
- ... and of elicitation methods = let participants explain their rationale

Levels of Reasoning in Keynesian Beauty Contests: A Generative Framework

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q ... and of elicitation methods = let participants explain their rationale
My outsider’s view

- Huge progress has been made to bring experimental insights to macro
- For instance: Angeletos, Benhabib, Duffy, Nagel and co-authors

- Body of experimental evidence gives rich description of decision-making in the lab and the field
- **Tougher:** incorporating into theoretical models: heterogeneity, aggregation, prediction

- Have we got closer to being able to “predict the next crisis”?

- Building robust institutions to support the macroeconomy:
- Culture and institutions (Alesina & Giuliano, JEL 2015)
Discussion of

The Case for Knightian Uncertainty: Rationality and Psychology in Macroeconomics and Finance Theory

Roman Frydman, Søren Johansen, Anders Rahbek, Morten Nyboe Tabor

by Sascha O. Becker
Knightian uncertainty

- Frank Knight: “There is a fundamental distinction between the reward for taking a *known risk* and that for assuming a *risk whose value itself is not known*.” A known risk is “easily converted into an effective certainty,” while “true uncertainty,” as Knight called it, is “not susceptible to measurement.”

- Wikipedia: “… there is no single best formal system of probability and belief to represent Knightian uncertainty. Economists and management scientists continue to look at practical methodologies for decision under different types of uncertainty.”

- **New concept**: Knightian Uncertainty Expectations (KUE)
Qualitative instead of quantitative conditions

- Imposing consistency in a model that recognizes that an economist faces Knightian uncertainty yields neither precise nor uniform representations of participants’ rationality in forecasting.

- … formalized at best with **qualitative** mathematical conditions.

- Dividends $b_t$, and time-varying drift coefficient of log earnings $x$:

  $$ b_t \in [b_-, b_+] , \text{ and } 0 < b_- < b_+ , $$

  $$ \mu_t \in [\mu_-, \mu_+] . $$
Qualitative conditions instead of quantitative ones (II)

- Model features “white noise risk” \( \mathcal{E}_{d,t+k} \)

- … and “true uncertainty” is reflected by interval \( I_{t:t+k}^b x_{t+k} \)

- Model predictions are not point estimates for \( d_{t+k} \)

- Instead: KU intervals as “uncertainty expected (UE)” intervals for \( d_{t+k} \)
Bounds & confidence intervals

- Econometrics of “uncertainty expected (UE)” intervals:
- If point estimates are replaced by intervals (“bounds”), how about standard errors: confidence bands around bounds?
“Predicting” history?

- Could we have predicted previous crises, had our models incorporated Knightian uncertainty?