



the institute for
advanced studies



Limits to Rationality in Financial Markets

June 15th to July 3rd, 2009

The standard efficient market models claim that trading in financial markets is driven by cognitive processes involving the maximisation of risk-adjusted returns, with arbitrage ensuring that the resulting prices are efficient in the sense of reflecting all the relevant available information, and the resulting return distributions following Gaussian statistics. However, even the very language of financial markets, such as "bulls and bears", "market sentiment" and so on, suggests that affective processes play an important role. The observed return distributions exhibit fat tails, clustered volatility, long-term memory and other features that can potentially result in financial crises damaging the economy as a whole (as is seen in the current "credit crunch"). The challenges then are to construct tests for the presence of affective processes in the behaviour of agents in financial markets, analyse the interaction of such affective processes with cognitive processes, and model how the choices at the micro-level interact to produce the non-Gaussian statistics observed at the macro-level.

Part of the IAS "Limits to Rationality in Economics Programme," this three week long workshop is designed to initiate a series of parallel research projects, facilitate interactions across traditional academic boundaries and involve practitioners and policy makers. We will consider the relevant areas in two day slots, leaving Wednesday of each week free for discussions.

Week 1:

15-16 June **Philosophical Issues**
18-19 June **Neuroeconomics**

Week 2:

22-23 June **Economic Analysis**
25-26 June **Experiments in Financial Markets**

Week 3:

29-30 June **Mathematical Modelling**
2-3 July **Policy implications and Closing**

The workshop will also include a public lecture (by P. Ormerod) and the closing address will be given by the Scottish First Minister, Alex Salmond. Details of other invited participants can be found on the Institute for Advanced Studies website. As well as a number of invited participants, the programme organisers welcome applications to attend and participate. There is no registration fee for the workshop and we are able to cover some travel and accommodation costs of the attendees. Contact one of the organisers for further details: Rod Cross (rod.cross@strath.ac.uk), Michael Grinfeld (michael@maths.strath.ac.uk) and Harbir Lamba (hlamba@gmu.edu).

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