

# How Learning in Financial Markets Generates Excess Volatility and Predictability in Stock Prices

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## Abstract

Two of the most discussed anomalies in the financial literature are the predictability of excess returns and the excess volatility of stock prices. Learning effects on stock price dynamics are an intuitive candidate to explain these empirical findings: estimation uncertainty may increase volatility of stock prices and an estimate of the dividend growth rate that is, say, lower than the “true” value tends to increase the dividend yield and capital gain. Simulations of learning effects in a present value model confirm that learning may help to explain excess volatility and predictability of stock returns.

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