

[Home](#) > [Eastern Economic Journal](#) > [Article](#)

The Impact of Imitation on Long Memory in an Order-Driven Market

| Symposium Article | Published: 02 November 2008

| Volume 34, pages 504–517, (2008) [Cite this article](#)

[Eastern Economic Journal](#)

[Aims and scope](#) →[Submit manuscript](#) →[Blake LeBaron¹](#) & [Ryuichi Yamamoto²](#) 101 Accesses 33 Citations [Explore all metrics](#) →

Abstract

Recent research has documented that learning and evolution are capable of generating many well-known features in financial times series. We extend the results of LeBaron and Yamamoto (2007) to explore the impact of varying amounts of imitation and agent learning in a simple order-driven market. We show that in our framework, imitation is critical to the generation of long memory persistence in many financial time series. This shows that imitation across trader behavior is probably crucial for understanding the dynamics of prices and trading volume.

This is a preview of subscription content, [log in via an institution](#) to check access.

[Access this article](#)

[Log in via an institution →](#)

[Buy article PDF 39,95 €](#)

Price includes VAT (Poland)

Instant access to the full article PDF.

Rent this article via [DeepDyve](#) [↗](#)

[Institutional subscriptions](#) →

Similar content being viewed by others



[Asymmetric Information and Learning by Imitation in Agent-Based Financial Markets](#)

Chapter | © 2019



[Agent-Based Modelling of Stock Markets Using Existing Order Book Data](#)

Chapter | © 2013



[Testing Adaptive Expectations Models of a Continuous Double Auction Market against Empirical Facts](#)

Chapter | © 2013

Notes

1. We are grateful to four anonymous referees who provided useful suggestions and feedback. Barkley Rosser provided useful comments on the authors' earlier work that inspired the research questions addressed in this paper.
2. See [LeBaron \[2001b\]](#) for an example of how endogenously changing heterogeneity in investor strategies can impact observed market behavior.
3. See [Khandani and Lo \[2007\]](#) for information on how this situation might occur

with quantitative hedge funds.

4. The use of k here represents a crude form of heterogeneous risk aversion in our population. Both buyers and sellers demand some premium beyond their risk neutral price. In this sense we are assuming that the actual risk of placing the order dominates any impact on the agents' portfolio. As a practical matter this also keeps traders from churning their portfolios at the same buy and sell prices. We model k as symmetric since we are not modeling any specific differences between buying and selling behavior. Also, there is some empirical evidence on the symmetry of order placement in [Mike and Farmer \[2008\]](#).
5. We have performed robustness checks on our mutation rate. For values of $p_m = 0, 0.08, 0.12, 0.16$ our results are unchanged. As the mutation rate gets very high, the selective impact of the GA is driven to zero, and the results will disappear for relatively large values of p_m . We have performed further robustness checks on other parameters used in our simulations. Specifically, we have varied σ_1 , the standard deviation of the fundamental forecasts from 0.5 to 1.5 from our original value of 1. We have also varied σ_2 the chartist forecasting component from 1 to 2 from the original value of 1.5, and the noise standard deviation, σ_n , from 0.3 to 0.7 from our original value of 0.5. Finally, we have adjusted k_{max} , the spread parameter length from 0.3 to 0.7. In all these cases we find that our results do not change significantly.
6. See [Vriend \[2000\]](#) for a general discussion.
7. It is beyond the scope of this paper to discuss long-memory processes. Interested readers should consult some recent surveys which include [Baillie \[1996\]](#), [Robinson \[2003\]](#), and [Doukhan et al. \[2003\]](#). See also [Parke \[1999\]](#) for examples, intuition and discussion. Recent work in finance shows that volatility is a likely candidate for long memory even at longer horizons than intraday. For examples see [Ding et al. \[1993\]](#), [Baillie et al. \[1996\]](#), and [Andersen et al. \[2003\]](#).

8. The Lo test is one of many long memory tests, and is based on earlier R/S analysis. The test has been criticized in [Teverosvsky et al. \[1999\]](#) and [Willinger et al. \[1999\]](#). Their Monte-Carlo experiments show that the test can accept the null of no long-range dependence as the bandwidth parameter is increased. We are concerned about this, but in most of our runs this low power problem is not an issue since we are rejecting the null hypothesis. We are also exploring the use of some other long-range diagnostics such as [Giraitis et al. \[2003a, 2003b\]](#).
9. We have also experimented with smaller order blocks, specifically 10 units. These blocks were not able to generate long memory in any of our time series. Obviously, there are many ways to implement order splitting, and we are continuing to explore the differences between these mechanisms, and our imitative framework.

References

Andersen, Torben G., Tim Bollerslev, Francis X. Diebold, and Paul Labys . 2003. Modeling and Forecasting Realized Volatility. *Econometrica*, 96: 579-625.

[Article](#) [Google Scholar](#)

Arthur, W.Brian, John Holland, Blake LeBaron, Richard Palmer, and Paul Tayler . 1997. Asset Pricing Under Endogenous Expectations in an Artificial Stock Market, in *The Economy as an Evolving Complex System II*, edited by W. Brian Arthur, Steven N. Durlauf, and David A. Lane, Reading, MA: Addison-Wesley, 15-44.

[Google Scholar](#)

Baillie, Richard T., T. Bollerslev, and H.-O. Mikkelsen . 1996. Fractionally Integrated Generalized Autoregressive Conditional Heteroskedasticity. *Journal of Econometrics*, 74: 3-30.

Baillie, Richard T . 1996. Long Memory Processes and Fractional Integration in Econometrics. *Journal of Econometrics*, 73: 5-59.

[Article](#) [Google Scholar](#)

Bouchaud, Jean-Philippe, Yuval Gefen, Marc Potters, and Matthieu Wyart . 2004. Fluctuations and Response in Financial Markets: The Subtle Nature of 'random' Price Changes. *Quantitative Finance*, 4: 176-190.

[Article](#) [Google Scholar](#)

Chen, Shu-Heng, and Chia-Hsuan Yeh . 2001. Evolving Traders and the Business School with Genetic Programming: A New Architecture of the Agent-based Artificial Stock Market. *Journal of Economic Dynamics and Control*, 25: 363-394.

[Article](#) [Google Scholar](#)

Chiarella, Carl, and Giulia Iori . 2002. A Simulation Analysis of the Microstructure of Double Auction Markets. *Quantitative Finance*, 2: 346-353.

[Article](#) [Google Scholar](#)

Chiarella, Carl, Giulia Iori, and Josep Perello . 2004. The Impact of Heterogeneous Trading Rules on the Limit Order Book and Order Flows, Technical Report, Department of Economics, City University London.

Cohen, Kalman J., Steven F. Maier, Robert A. Schwartz, and David K. Whitcomb . 1983. A Simulation Model of Stock Exchange Trading. *Simulation*, 41: 181-191.

[Article](#) [Google Scholar](#)

Ding, Zhuanxin, Clive W.J. Granger, and Robert F. Engle . 1993. A Long Memory

Property of Stock Market Returns and a New Model. *Journal of Empirical Finance*, 1: 83-106.

[Article](#) [Google Scholar](#)

Domowitz, Ian, and Jianxin Wang . 1994. Auctions as Algorithms: Computerized Trade Execution and Price Discovery. *Journal of Economic Dynamics and Control*, 18: 29-60.

[Article](#) [Google Scholar](#)

Doukhan, Paul, George Oppenheim, and Murad Taqqu . 2003. *Theory and Applications of Long Range Dependence*. Basel: Birkhauser.

[Google Scholar](#)

Farmer, J.Doyne, Paolo Patelli, and Ilija Zovko . 2005. The Predictive Power of Zero Intelligence Models in Financial Markets. *Proceedings of the National Academy of Sciences of the United States of America*, 102: 2254-2259.

[Article](#) [Google Scholar](#)

Giraitis, Liudas, Piotr Kokosza, Remigijus Leipus, and Gilles Teyssiere . 2003a. Rescaled Variance and Related Tests for Long Memory in Volatility and Levels. *Journal of Econometrics*, 112: 265-294.

[Article](#) [Google Scholar](#)

Giraitis, Liudas, Piotr Kokosza, Remigijus Leipus, and Gilles Teyssiere . 2003b. On the Power of R/S Type Tests Under Contiguous and Semi-long Memory Alternatives. *Acta Applicandae Mathematicae*, 78: 285-299.

[Article](#) [Google Scholar](#)

Gode, Dhananjay K., and Shyam Sunder . 1993. Allocative Efficiency of Markets

with Zero Intelligence Traders. *Journal of Political Economy*, 101: 119–137.

[Article](#) [Google Scholar](#)

Goettler, R., C.A. Parlour, and U. Rajan . 2005. Equilibrium in a Dynamic Limit Order Market. *Journal of Finance*, 60: 2149–2192.

[Article](#) [Google Scholar](#)

Granger, Clive W . 1980. Long Memory Relationships and the Aggregation of Dynamic Models. *Journal of Econometrics*, 14: 227–238.

[Article](#) [Google Scholar](#)

Khandani, Amir, and Andrew W. Lo . 2007. What Happened to the Quants in August 2007? *Journal of Investment Management*, 5: 29–78.

[Google Scholar](#)

Ladley, Dan, and Klaus R. Schenk-Hoppe . 2007. Do Stylized Facts of Order Book Markets Need Strategic Behavior, Technical Report, University of Leeds.

LeBaron, Blake . 2001a. Evolution and Time Horizons in an Agent Based Stock Market. *Macroeconomic Dynamics*, 5 (2): 225–254.

[Article](#) [Google Scholar](#)

LeBaron, Blake . 2001b. Financial Market Efficiency in a Coevolutionary Environment, in *Proceedings of the Workshop Simulation of Social Agents: Architectures and Institutions*, edited by David Sallach and Thomas Wolsko, Argonne National Laboratories, Argonne, IL: pp. 33–51.

[Google Scholar](#)

LeBaron, Blake, and Ryuichi Yamamoto . 2007. Long-memory in an Order-driven

Market. *Physica A*, 383: 85–89.

[Article](#) [Google Scholar](#)

Lillo, Fabrizio, and J. Doyne Farmer . 2004. The Long Memory of the Efficient Market. *Studies in Nonlinear Dynamics and Econometrics*, 8 (3): 1–32.

[Google Scholar](#)

Lillo, Fabrizio, Szabolcs Mike, and J. Doyne Farmer . 2005. Theory for Long Memory in Supply and Demand. *Physica Review E*, 7106: 287–297.

[Google Scholar](#)

Lo, Andrew W. 1991. Long-Term Memory in Stock Market Prices. *Econometrica*, 59: 1279–1314.

[Article](#) [Google Scholar](#)

Mike, Szabolcs, and J. Doyne Farmer . 2008. An Empirical Behavioral Model of Liquidity and Volatility. *Journal of Economic Dynamics and Control*, 32: 200–234.

[Article](#) [Google Scholar](#)

Parke, William R . 1999. What is Fractional Integration? *Review of Economics and Statistics*, 81 (4): 632–638.

[Article](#) [Google Scholar](#)

Robinson, Peter M . 1978. Statistical Inference for a Random Coefficient Autoregressive Model. *Scandinavian Journal of Statistics*, 5: 163–168.

[Google Scholar](#)

Robinson, Peter M . 2003. Long Memory Time Series, in *Time Series with Long*

Teverosvsky, Vadim, Murad Taqqu, and Walter Willinger . 1999. A Critical Look at Lo's Modified R/S Statistic. *Journal of Statistical Planning and Inference*, 80: 211-227.

[Article](#) [Google Scholar](#)

Vriend, Nicolaas J . 2000. An Illustration of the Essential Difference Between Individual and Social Learning, and its Consequences for Computational Analysis. *Journal of Economic Dynamics and Control*, 24: 1-19.

[Article](#) [Google Scholar](#)

Willinger, Walter, Murad Taqqu, and Vadim Teverosvsky . 1999. Stock Market Prices and Long Range Dependence. *Finance and stochastics*, 3: 1-13.

[Article](#) [Google Scholar](#)

Author information

Authors and Affiliations

**International Business School, Brandeis University, 415 South Street,
Mailstop 32, Waltham, 02453-2728, MA, USA**

Blake LeBaron

**Department of International Business, National Chengchi University, 64
Sec.2, Zhi-Nan Road, Taipei, Taiwan**

Ryuichi Yamamoto

Rights and permissions

About this article

Cite this article

LeBaron, B., Yamamoto, R. The Impact of Imitation on Long Memory in an Order-Driven Market. *Eastern Econ J* **34**, 504–517 (2008). <https://doi.org/10.1057/eej.2008.32>

Published

02 November 2008

DOI

<https://doi.org/10.1057/eej.2008.32>

Issue Date

01 October 2008

Keywords

[learning](#)

[evolution](#)

[market microstructure](#)

[long memory](#)

JEL Classifications

[G12](#)

[G14](#)

[D83](#)

Search

Search by keyword or author



Navigation

Find a journal

Publish with us

