

HETEROGENEOUS AGENTS AND THE COLLAPSE OF AN EXCHANGE RATE REGIME

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ABSTRACT

This paper argues that the form of speculative attacks on currencies is inextricably tied to the nature of heterogeneity of speculators. Heterogeneity of speculators, derived from differences in relative risk aversion, differences in information sets, and nonuniformity in liquidity or market power may lead to a spectrum of expectations and stimuli response patterns. Under such circumstances a balance of payments crisis can be characterized by a series of mini-speculative attacks on a currency. Attacks by groups of agents need not succeed at collapsing a fixed exchange rate as implied by the representative or homogeneous agent models. Speculative attacks on a currency are a function of the estimated mean and uncertainty surrounding expected post-collapse gains. The probability of collapsing an exchange rate regimes depends on the liquidity of attacking agents and on the responses and mutual perceptions of heterogeneous speculators. Balance of payments crises need not be self-fulfilling events.

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