

An Experimental Study of Money Illusion in Intertemporal Decision Making

Abstract

To examine the effects of price fluctuations on the individual behavior in a problem of intertemporal decision making, we conducted a laboratory experiment in which the subjects spend their savings for consumptions over 20 periods. In the control treatment, the price of the commodity is constant during the entire periods. In the small (large) fluctuation treatment, the price rate of change is always 1% (20%). The rate of change of the savings is always the same as the commodity price. Therefore, the optimal amount of consumption is the same in all three treatments. The experimental results robustly show that subjects in the small fluctuation treatment are more likely to mispurchase (deviate from the optimal consumption) than in the control treatment. The results also show that the volume of the mispurchase in the control and large fluctuation treatments shrinks over time, whereas that in the small fluctuation treatment gradually increases.