

SUPPLEMENT TO “SAVAGE IN THE MARKET”
(*Econometrica*, Vol. 83, No. 4, July 2015, 1467–1495)

BY FEDERICO ECHENIQUE AND KOTA SAITO

THIS SUPPLEMENT CONSISTS OF EIGHT SECTIONS.

In Section S.1, we illustrate the use of SARSEU through a few simple theoretical exercises. In each case, the exercise is to present a well known alternative to risk-averse SEU and to show that data generated by these theories can violate SARSEU.

In Section S.2, we show that, in the 2×2 case, SARSEU is equivalent to requirements (5) and (6) in the main paper.

In Section S.3, we provide the details of the example of risk-averse probability sophisticated preferences that violate SARSEU.

In Section S.4, we present the proof of Proposition 6, on the equivalence between SEU rationality and maxmin expected utility rationality.

In Section S.5, we show that SEU and SDU are observationally equivalent under certain assumptions on the data.

In Section S.6, we present the relationship between SARSEU and results obtained in the revealed preference literature on *objective* expected utility, where the probability over states is assumed to be observable and given as a primitive. The point is that the axiom to characterize objective expected utility has a similar syntax to SARSEU and that the differences between the two are instructive.

In Section S.7, we present the proof of Theorem 22 in Appendix B of the paper. The theorem is a generalization of Section S.6 and the main result in the paper (Theorem 1) in the sense that we allow that there are some states whose probabilities are objective and known to us.

In Section S.8, we study the relation between SARSEU and the axiomatization in [Savage \(1954\)](#). It is useful to see the role of SARSDU and SARSEU in ruling out violations of Savage’s axioms.

S.1. APPLICATIONS OF SARSEU

We discuss, in turn, nonconcave SEU and SDU. By showing that these models can generate data sets that violate SARSEU, we show that the models are in fact testable beyond risk-averse SEU. In other words, that nonconcave SEU and SDU all have testable implications over and beyond those of risk-averse SEU. This point has been made by Bayer, Bose, Polisson, and Renou (2012) for nonconcave SEU and maxmin expected utility, but they use Afriat inequalities to this end; here we seek to illustrate the use of SARSEU.

S.1.1. *Nonconcave SEU*

The concavity of u plays an important role in our characterization. This should not be surprising, as risk aversion has obvious economic meaning and

content. There are, however, instances in revealed preference theory where concavity has no implications for a rational consumer. Afriat's theorem (Afriat (1967)) shows that concavity is not a testable property of a utility function. For the SEU model, concavity of u is equivalent to the convexity of preferences over state-contingent bundles. So it is legitimate to ask about the testability of the concavity of u . In this section, we show that indeed concavity is testable.

In the following, we will show an example of a data set generated from a nonconcave SEU model that violates SARSEU.

Consider the data set

$$p^{k_1} = (1, 2), \quad x^{k_1} = (1, 2) \quad \text{and} \quad p^{k_2} = (1.1, 2), \quad x^{k_2} = (10, 1).$$

Note that

$$x_{s_2}^{k_1} > x_{s_2}^{k_2} \quad \text{and} \quad x_{s_1}^{k_2} > x_{s_1}^{k_1},$$

while

$$\frac{p_{s_2}^{k_1} p_{s_1}^{k_2}}{p_{s_2}^{k_2} x_{s_1}^{k_1}} = \frac{2 \cdot 1.1}{2 \cdot 1} = 1.1 > 1,$$

so SARSEU is violated, and the data set is not rationalizable by any concave utility and priors.

It is, however, rationalizable by the following nonconcave SEU. Let $\mu = (\frac{1}{3}, \frac{2}{3})$. Define

$$v(x) = \begin{cases} 1 & \text{if } x \leq 9, \\ 2 & \text{if } 9 < x \leq 10, \\ 1 & \text{if } x > 10. \end{cases}$$

Remember that $B(p, I) = \{x \in \mathbf{R}_+^2 : p^k \cdot x \leq p^k \cdot x^k \text{ for all } p \in \mathbf{R}_{++}^S \text{ and } I \in \mathbf{R}_{++}\}$. Let $u(x) = \int_0^x v(s) ds$.

It is clear that x^1 is optimal for $\sum \mu_s u(x_s)$ in $B(p^1, p^1 \cdot x^1)$, as $v(x_{s_1}) = v(x_{s_2}) = 1$ for all $(x_{s_1}, x_{s_2}) \in B(p^1, p^1 \cdot x^1)$.

By the monotonicity of u , any maximum of $\sum \mu_s u(x_s)$ in $B(p^2, p^2 \cdot x^2)$ must lie on the budget line $p_{s_1}^{k_2} x_{s_1} + p_{s_2}^{k_2} x_{s_2} = 13$. Note that, on the budget line,

$$x_{s_2} = \frac{13 - 1.1x_{s_1}}{2},$$

so $x_{s_2} \leq \frac{13}{2} < 9$ for $x_{s_1} \geq 0$. For all $x_{s_1} \geq 0$, define $f(x_{s_1}) = \mu_1 u(x_{s_1}) + \mu_2 u(x_{s_2}) = \frac{1}{3}[u(x_{s_1}) + 2u(\frac{13-1.1x_{s_1}}{2})]$. Then $f'(x_{s_1}) = \frac{1}{3}[v(x_{s_1}) - 1.1]$ for $x_{s_1} \in [0, 13/1.1]$, as

$v(\frac{13-1.1x_{s_1}}{2}) = 1$. Thus,

$$f'(x_{s_1}) = \begin{cases} \frac{-0.1}{3} & \text{if } x_{s_1} \leq 9, \\ \frac{0.9}{3} & \text{if } 9 < x_{s_1} \leq 10, \\ \frac{-0.1}{3} & \text{if } 10 < x_{s_1}. \end{cases}$$

So $f(x_{s_1})$ has two local maxima, $x_{s_1} = 0$ and $x_{s_1} = 10$. By a direct calculation, $f(0) = \frac{13}{6} = 2 + \frac{1}{6}$ and $f(10) = \frac{1}{3}(9 + 2) + \frac{2}{3}(\frac{13-1.1 \times 10}{2}) = 3 + \frac{4}{3}$. Since $f(10) > f(0)$, it is indeed optimal to choose x^2 in $B(p^2, p^2 \cdot x^2)$.

S.1.2. State-Dependent Utility

SDU is the model in which an agent seeks to maximize $\sum_{s \in S} u_s(x_s)$, where u_s is a utility function over money for each state s . By means of Afriat inequalities, [Varian \(1983a\)](#) has proposed a characterization of an additive linear model that includes a SDU model as a special case.

On the other hand, we have proposed a combinatorial axiom (i.e., SARSDU) for concave SDU, which is beyond Afriat inequalities. The axiom is weaker than SARSEU. Hence, the two models should be distinguishable. In the following discussion, we propose an example of a data set that is consistent with SARSDU but not with SARSEU.

Assume $S = \{s_1, s_2\}$. Consider the data set

$$p^{k_1} = (3, 2), \quad p^{k_2} = (1, 1) \quad \text{and} \quad x^{k_1} = (2, 1), \quad x^{k_2} = (3, 4).$$

Choose strictly concave functions u_{s_1} and u_{s_2} such that

$$u'_{s_1}(2) = 3 > 1 = u'_{s_1}(3) \quad \text{and} \quad u'_{s_2}(1) = 2 > 1 = u'_{s_2}(4).$$

Then

$$\frac{u'_{s_1}(2)}{u'_{s_2}(1)} = \frac{p^{k_1}_{s_1}}{p^{k_1}_{s_2}}, \quad \frac{u'_{s_1}(3)}{u'_{s_2}(4)} = \frac{p^{k_2}_{s_1}}{p^{k_2}_{s_2}},$$

so that the first-order conditions are satisfied.

The sequence $\{(x^{k_1}_{s_1}, x^{k_1}_{s_2}), (x^{k_2}_{s_2}, x^{k_2}_{s_1})\}$ satisfies the condition of SARSEU. However,

$$\frac{p^{k_1}_{s_1} p^{k_2}_{s_2}}{p^{k_1}_{s_2} p^{k_2}_{s_1}} = \frac{3}{2} > 1.$$

This is a violation of SARSEU. Note also that this data set violates requirement (6).

S.2. PROOF OF REMARK 1

In Remark 1 in the paper, we claimed that the following two requirements are equivalent to SARSEU in the 2×2 case. Here we prove this statement.

REQUIREMENTS:

$$(5) \quad x_{s_1}^{k_1} > x_{s_1}^{k_2} \quad \text{and} \quad x_{s_2}^{k_2} > x_{s_2}^{k_1} \quad \Rightarrow \quad \frac{p_{s_1}^{k_1} p_{s_2}^{k_2}}{p_{s_1}^{k_2} p_{s_2}^{k_1}} \leq 1,$$

$$(6) \quad x_{s_1}^{k_1} > x_{s_2}^{k_1} \quad \text{and} \quad x_{s_2}^{k_2} > x_{s_1}^{k_2} \quad \Rightarrow \quad \frac{p_{s_1}^{k_1} p_{s_2}^{k_2}}{p_{s_2}^{k_1} p_{s_1}^{k_2}} \leq 1.$$

REMARK: In the 2×2 case, a data set satisfies SARSEU if and only if it satisfies requirements (5) and (6).

PROOF: It is easy to see that SARSEU implies the two requirements. To prove the reciprocal, we need a preliminary concept.

We say that a set $\sigma \equiv \{(x_{s_i}^{k_i}, x_{s'_i}^{k'_i})\}_{i=1}^n$ of pairs that satisfies the three conditions in SARSEU is *minimal* if there exists no subset $(\sigma_i)_{i=1}^m$ of pairs such that (i) σ_i satisfies the three conditions in SARSEU for each $i = 1, \dots, m$ and (ii) $\sigma = \bigcup_{i=1}^m \sigma_i$.

STEP 1: If a set $\{(x_{s_i}^{k_i}, x_{s'_i}^{k'_i})\}_{i=1}^n$ of pairs is minimal and satisfies the three conditions, then it must take one of the following forms:

- (a) $\sigma^a \equiv \{(x_{s_1}^{k_1}, x_{s_2}^{k_1}), (x_{s_2}^{k_2}, x_{s_1}^{k_2})\}$;
- (b) $\sigma^b \equiv \{(x_{s_1}^{k_1}, x_{s_1}^{k_2}), (x_{s_2}^{k_2}, x_{s_2}^{k_1})\}$;
- (c) $\sigma^c \equiv \{(x_s^k, x_{s'}^{k'}), (x_{s'}^{k'}, x_s^k), (x_{s'}^{k'}, x_s^{k'})\}$ for some k, k' such that $k \neq k'$ and s, s' such that $s \neq s'$;
- (d) $\sigma^d \equiv \{(x_s^k, x_{s'}^{k'}), (x_s^{k'}, x_s^k), (x_s^k, x_{s'}^{k'})\}$ for some k, k' such that $k \neq k'$ and s, s' such that $s \neq s'$.

PROOF: Fix a minimal set $\sigma = \{(x_{s_i}^{k_i}, x_{s'_i}^{k'_i})\}_{i=1}^n$ of pairs that satisfies the three conditions.

CASE 1: For all i , either $k_i = k'_i$ or $s_i = s'_i$ holds. It is easy to see that either $\sigma = \{(x_{s_1}^{k_1}, x_{s_2}^{k_1}), (x_{s_2}^{k_2}, x_{s_1}^{k_2})\}$ or $\sigma = \{(x_{s_1}^{k_1}, x_{s_1}^{k_2}), (x_{s_2}^{k_2}, x_{s_2}^{k_1})\}$. These correspond to Step 1(a) and (b).

CASE 2: There exists i such that neither $k_i = k'_i$ nor $s_i = s'_i$ holds. Suppose that we have $(x_{s_1}^{k_1}, x_{s_2}^{k_2})$ in the pair without loss of generality.

We cannot have $(x_{s_2}^{k_2}, x_{s_1}^{k_1})$ in σ because of condition (i). Since the sequence $\{(x_{s_i}^{k_i}, x_{s'_i}^{k'_i})\}_{i=1}^n$ satisfies conditions (ii) and (iii), we must have two pairs such that $(x_{s_2}^{k_2}, x_s^{k_1})$ and $(x_s^k, x_{s_1}^k)$ for some $s \in \{s_1, s_2\}$ and $k \in \{k_1, k_2\}$ in the sequence.

Note that we cannot have $(x_{s_2}^{k_2}, x_{s_2}^{k_1})$ and $(x_{s_2}^{k_1}, x_{s_1}^{k_1})$ because these imply $x_{s_2}^{k_2} > x_{s_2}^{k_1} > x_{s_1}^{k_1}$, which would contradict that $(x_{s_1}^{k_1}, x_{s_2}^{k_2})$ in σ satisfies condition (i).

Note also that we cannot have $(x_{s_1}^{k_2}, x_{s_1}^{k_1})$ and $(x_{s_2}^{k_2}, x_{s_1}^{k_2})$ because these imply $x_{s_2}^{k_2} > x_{s_1}^{k_2} > x_{s_1}^{k_1}$. This again contradicts that $(x_{s_1}^{k_1}, x_{s_2}^{k_2})$ in σ satisfies condition (i). It follows that we must have one of the following two subcases.

SUBCASE 2.1: The pairs $(x_{s_2}^{k_2}, x_{s_2}^{k_1})$ and $(x_{s_2}^{k_2}, x_{s_1}^{k_2})$ are in σ . Then $\{(x_{s_1}^{k_1}, x_{s_2}^{k_2}), (x_{s_2}^{k_2}, x_{s_2}^{k_1}), (x_{s_2}^{k_2}, x_{s_1}^{k_2})\}$ satisfies the three conditions. Since σ is minimal, it must hold that $\sigma = \{(x_{s_1}^{k_1}, x_{s_2}^{k_2}), (x_{s_2}^{k_2}, x_{s_2}^{k_1}), (x_{s_2}^{k_2}, x_{s_1}^{k_2})\}$. This corresponds to Step 1(c).

SUBCASE 2.2: The pairs $(x_{s_1}^{k_2}, x_{s_1}^{k_1})$ and $(x_{s_2}^{k_1}, x_{s_1}^{k_1})$ are in σ . In this case, again by the minimality of σ , it must hold that $\sigma = \{(x_{s_1}^{k_1}, x_{s_2}^{k_2}), (x_{s_1}^{k_2}, x_{s_1}^{k_1}), (x_{s_2}^{k_1}, x_{s_1}^{k_1})\}$. This corresponds to Step 1(d).

Note that we have exhausted all cases.

Q.E.D.

For any set $\sigma \equiv \{(x_{s_i}^{k_i}, x_{s'_i}^{k'_i})\}_{i=1}^n$ of pairs that satisfies the three conditions in SARSEU, define

$$f(\sigma) = \prod_{i=1}^n \frac{p_{s_i}^{k_i}}{p_{s'_i}^{k'_i}}.$$

STEP 2: We have $f(\sigma^t) \leq 1$ for each $t \in \{a, b, c, d\}$.

PROOF: By requirement (5),

$$f(\sigma^a) = \frac{p_{s_1}^{k_1} p_{s_2}^{k_2}}{p_{s_1}^{k_2} p_{s_2}^{k_1}} \leq 1.$$

By requirement (6),

$$f(\sigma^b) = \frac{p_{s_1}^{k_1} p_{s_2}^{k_2}}{p_{s_2}^{k_1} p_{s_1}^{k_2}} \leq 1.$$

To show that $f(\sigma^c) \leq 1$, assume without loss of generality that $\sigma^c = \{(x_{s_1}^{k_1}, x_{s_2}^{k_2}), (x_{s_2}^{k_2}, x_{s_1}^{k_1}), (x_{s_2}^{k_2}, x_{s_1}^{k_2})\}$. In this case, it must hold that $x_{s_2}^{k_2} > x_{s_1}^{k_2}$ and $x_{s_1}^{k_1} > x_{s_2}^{k_1}$. Hence, by requirement (6),

$$\frac{p_{s_2}^{k_2} p_{s_1}^{k_1}}{p_{s_1}^{k_2} p_{s_2}^{k_1}} \leq 1.$$

So

$$f(\sigma^c) = \frac{p_{s_1}^{k_1} p_{s_2}^{k_2} p_{s_2}^{k_2}}{p_{s_2}^{k_2} p_{s_1}^{k_1} p_{s_1}^{k_2}} = \frac{p_{s_2}^{k_2} p_{s_1}^{k_1}}{p_{s_1}^{k_2} p_{s_2}^{k_1}} \leq 1.$$

To show that $f(\sigma^d) \leq 1$, assume without loss of generality that $\sigma^d = \{(x_{s_1}^{k_1}, x_{s_2}^{k_2}), (x_{s_1}^{k_2}, x_{s_1}^{k_1}), (x_{s_2}^{k_2}, x_{s_1}^{k_1})\}$. In this case, it must hold that $x_{s_1}^{k_2} > x_{s_2}^{k_2}$ and $x_{s_2}^{k_1} > x_{s_1}^{k_1}$. Hence, by requirement (6),

$$\frac{p_{s_1}^{k_2} p_{s_2}^{k_1}}{p_{s_1}^{k_2} p_{s_1}^{k_1}} \leq 1.$$

So

$$f(\sigma^d) = \frac{p_{s_1}^{k_1} p_{s_1}^{k_2} p_{s_2}^{k_1}}{p_{s_2}^{k_2} p_{s_1}^{k_1} p_{s_1}^{k_1}} = \frac{p_{s_1}^{k_2} p_{s_2}^{k_1}}{p_{s_2}^{k_2} p_{s_1}^{k_1}} \leq 1. \quad Q.E.D.$$

Now by using Steps 1 and 2, we can prove the remark. Choose a sequence of pairs $(x_{s_i}^{k_i}, x_{s_i'}^{k_i'})_{i=1}^n$ that satisfies the three conditions in SARSEU. Let $\sigma = \{(x_{s_i}^{k_i}, x_{s_i'}^{k_i'})_{i=1}^n\}$. For each t , there exists a set of index $M(t)$ such that $\sigma = (\bigcup_{i \in M(a)} \sigma^a) \cup (\bigcup_{i \in M(b)} \sigma^b) \cup (\bigcup_{i \in M(c)} \sigma^c) \cup (\bigcup_{i \in M(d)} \sigma^d)$:

$$\prod_{i=1}^n \frac{p_{s_i}^{k_i}}{p_{s_i'}^{k_i'}} = f(\sigma) = \left(\prod_{i \in M(a)} f(\sigma^a) \right) \cdots \left(\prod_{i \in M(d)} f(\sigma^d) \right) \leq 1. \quad Q.E.D.$$

S.3. PROBABILISTIC SOPHISTICATED

We present the detailed arguments behind the example in Section 5 of the paper. The example has a data set that is generated by risk-averse probability sophisticated preferences, but that violates SARSEU.

In the example, we have $S = \{s_1, s_2\}$ and $x^1 = (2, 2)$, $p^1 = (1, 2)$, $x^2 = (8, 0)$, and $p^2 = (1, 1)$. In the following discussion, we define the function V that represents the probabilistically sophisticated preferences. Fix $\mu \in \Delta_{++}$ with $\mu_{s_1} = \mu_{s_2} = 1/2$. Any vector $x \in \mathbf{R}_+^2$ induces the probability distribution on \mathbf{R}_+ given by x_1 with probability $1/2$ and x_2 with probability $1/2$. Let Π be the set

of all probability measures on \mathbf{R}_+ for which the support is finite and has cardinality smaller than or equal to 2.

We shall define a function $V : \Pi \rightarrow \mathbf{R}$ that represents probabilistically sophisticated preferences. We use $h : \{(x_1, x_2) \in \mathbf{R}_+^2 : x_1 \geq x_2\} \rightarrow \mathbf{R}$ with the property that

$$h(x_1, x_2) \leq h\left(\frac{x_1 + x_2}{2}, \frac{x_1 + x_2}{2}\right),$$

and then define $V(\pi) = h(\bar{x}^\pi, \underline{x}^\pi)$, where \underline{x}^π is the smallest point in the support of π and \bar{x}^π is the largest.

Let C_1 be the set of vectors x for which $x_1 + x_2 \geq 8$, let C_3 be the set of vectors x for which $x_1 + 2x_2 \leq 6$, and let C_2 be the complement of $C_1 \cup C_3$ in $\{(x_1, x_2) \in \mathbf{R}_+^2 : x_1 \geq x_2\}$. It is easy to see that these sets are pairwise disjoint.

For $\sigma \in (6, 8)$, let $l^\sigma \subset \mathbf{R}_+^2$ be the set of vectors on the line segment between (or the convex hull of) between $(\sigma, 0)$ and $(\sigma - 4, \sigma - 4)$. We have the following basic properties of σ .

LEMMA S.1: *Suppose that $\sigma \in (6, 8)$.*

(i) *We have $(x_1, x_2) \in l^\sigma$ if and only if*

$$x_2 = \left(\frac{\sigma - 4}{4}\right)(\sigma - x_1).$$

(ii) *We have $l^\sigma \subset C_2$.*

(iii) *For each $x \in C_2$, there is a unique $\sigma \in (6, 8)$ with $x \in l^\sigma$.*

PROOF: The proof of statement (i) is a direct calculation. For statement (ii), note that $\sigma < 8$ and $\sigma - 4 + \sigma - 4 < 8$. The function $(x_1, x_2) \mapsto x_1 + x_2$ is linear and is, therefore, maximized on l^σ at an extreme. Since this function is smaller than 8 on both extremes, it is smaller than 8 over all l^σ and, therefore, l^σ does not intersect C_1 . Similarly, it does not intersect C_3 by the linearity of $x_1 + 2x_2$ and checking the extremes.

For statement (iii), fix $\sigma \in (6, 8)$. Consider the function $f^\sigma(x_1, x_2) = (\sigma - 4)x_1 + 4x_2$. One can verify that $f^\sigma(\sigma, 0) = \sigma(\sigma - 4) = f^\sigma(\sigma - 4, \sigma - 4)$. Then $f^\sigma(x_1, x_2) = \sigma(\sigma - 4)$ for all $(x_1, x_2) \in l^\sigma$, as f^σ is linear. Consider $\sigma' \neq \sigma$. Say $\sigma' > \sigma$. Then the minimum of f^σ over $l^{\sigma'}$ is obtained at an extreme point of $l^{\sigma'}$, again by linearity. Now, $\sigma' > \sigma$ implies that $f^\sigma(\sigma, 0) < f^\sigma(\sigma', 0)$ and $f^\sigma(\sigma - 4, \sigma - 4) < f^\sigma(\sigma' - 4, \sigma' - 4)$. Hence, $f^\sigma(x) < f^\sigma(x')$ for all $x \in l^\sigma$ and $x' \in l^{\sigma'}$. Thus, if $x \in l^\sigma$, then $x \notin l^{\sigma'}$.

We complete the proof of statement (iii) by showing that for all $x \in C_2$ there is σ with $x \in l^\sigma$. Let $x \in C_2$. Consider the quadratic equation $\sigma^2 - (4 + x_1)\sigma + 4(x_1 - x_2) = 0$, derived from the identity in statement (i) of this lemma. By

solving this equation explicitly and choosing the larger solution, we obtain

$$\sigma = \frac{4 + x_1 + \sqrt{-8x_1 + x_1^2 + 16(1 + x_2)}}{2}.$$

By a direct calculation, it can be shown that

$$[\sigma > 6 \Leftrightarrow 6 < x_1 + 2x_2] \quad \text{and} \quad [\sigma < 8 \Leftrightarrow x_1 + 2x_2 > 6].$$

Since $x \in C^2$, we obtain $\sigma \in (6, 8)$.

Q.E.D.

Define the function $h : \{(x_1, x_2) \in \mathbf{R}_+^2 : x_1 \geq x_2\} \rightarrow \mathbf{R}$ as

$$h(x) = \begin{cases} \frac{1}{2}(x_1 + x_2) & \text{if } x \in C_1, \\ \frac{1}{3}(x_1 + 2x_2) & \text{if } x \in C_3, \\ \sigma(x_1, x_2) - 4 & \text{if } x \in C_2, \end{cases}$$

where $\sigma(x_1, x_2)$ is the unique $\sigma \in (6, 8)$ with $x \in l^\sigma$.

LEMMA S.2: *If $x \in C_3$, $x' \in C_2$, and $x'' \in C_1$, then $h(x) < h(x') < h(x'')$.*

PROOF: Let $\sigma \in \mathbf{R}_+$ be such that $x' \in l^\sigma$. We must have $8 > \sigma > 6$, so

$$h(x) = \frac{1}{3}(x_1 + 2x_2) \leq \frac{1}{3}6 < \sigma - 4 = h(x')$$

as $x_1 + 2x_2 \leq 6$ and $\sigma > 6$, and

$$h(x') = \sigma - 4 < 4 \leq \frac{1}{2}(x_1'' + x_2'') = h(x'')$$

as $8 > \sigma$ and $x_1'' + x_2'' \geq 8$.

Q.E.D.

LEMMA S.3: *For any $(x_1, x_2) \in \{(x_1, x_2) \in \mathbf{R}_+^2 : x_1 \geq x_2\}$,*

$$h(x_1, x_2) \leq h\left(\frac{x_1 + x_2}{2}, \frac{x_1 + x_2}{2}\right).$$

PROOF: First, let $x \in C_3$. If $(\frac{x_1+x_2}{2}, \frac{x_1+x_2}{2}) \notin C_3$, the result follows from Lemma S.2. So suppose that $(\frac{x_1+x_2}{2}, \frac{x_1+x_2}{2}) \in C_3$. Then

$$\begin{aligned} h\left(\frac{x_1 + x_2}{2}, \frac{x_1 + x_2}{2}\right) &= \frac{1}{3}\left(\frac{x_1 + x_2}{2} + x_1 + x_2\right) \geq \frac{1}{3}(x_1 + 2x_2) \\ &= h(x_1, x_2), \end{aligned}$$

where the inequality follows from $x_1 \geq x_2$.

Second, suppose that $x \in C_1$. Then $(\frac{x_1+x_2}{2}, \frac{x_1+x_2}{2}) \in C_1$ and it is immediate that $h(x) = h(\frac{x_1+x_2}{2}, \frac{x_1+x_2}{2})$.

Third, suppose that $x \in C_2$. It is easy to see that $(\frac{x_1+x_2}{2}, \frac{x_1+x_2}{2}) \notin C_3$ (as $\frac{x_1+x_2}{2} + 2\frac{x_1+x_2}{2} = x_1 + x_2 + \frac{x_1+x_2}{2} \geq x_1 + 2x_2 > 6$), and the result follows from Lemma S.2 when $(\frac{x_1+x_2}{2}, \frac{x_1+x_2}{2}) \in C_1$, so consider the case when $(\frac{x_1+x_2}{2}, \frac{x_1+x_2}{2}) \in C_2$.

Let $\sigma \in (6, 8)$ be such that $x \in l^\sigma$. Consider the function $(x'_1, x'_2) \mapsto x'_1 + x'_2$ for $(x'_1, x'_2) \in l^\sigma$. Note that $(x'_1, x'_2) \in l^\sigma$ means that

$$x'_1 + x'_2 = x'_1 + \frac{\sigma - 4}{4}(\sigma - x'_1) = \left(1 - \frac{\sigma - 4}{4}\right)x'_1 + \frac{\sigma - 4}{4}\sigma,$$

which is monotone increasing in x'_1 , as $\sigma < 8$. But $(x_1, x_2) \in l^\sigma$ implies that $x_1 \geq \sigma - 4$; hence, $(\sigma - 4) + (\sigma - 4) \leq x_1 + x_2$. Thus,

$$h(x) = \sigma - 4 \leq \frac{x_1 + x_2}{2} = h\left(\frac{x_1 + x_2}{2}, \frac{x_1 + x_2}{2}\right). \quad Q.E.D.$$

LEMMA S.4: *For all $x, x' \in \{(x_1, x_2) \in \mathbf{R}_+^2 : x_1 \geq x_2\}$, if $x'_2 \leq x_2$ and $x'_1 \leq x_1$, then $h(x'_1, x'_2) \leq h(x_1, x_2)$. If $x'_2 < x_2$ or $x'_1 < x_1$, furthermore, then $h(x'_1, x'_2) < h(x_1, x_2)$.*

PROOF: First $x \in C_1$. Then $x' \in C_1$ and there is nothing more to prove. In second place, suppose that $x \in C_2$. Then we cannot have $x' \in C_3$ as $x_1 + 2x_2 \leq x'_1 + 2x'_2$. The result follows from Lemma S.2 if $x' \in C_1$, so focus on the case when $x' \in C_2$. It suffices to show that $\sigma(x_1, x_2)$ is strictly increasing both in x_1 and in x_2 . As shown in the proof of Lemma S.3,

$$\sigma(x_1, x_2) = \frac{4 + x_1 + \sqrt{-8x_1 + x_1^2 + 16(1 + x_2)}}{2}.$$

By a direct calculation,

$$\frac{\partial \sigma}{\partial x_1} = \frac{1}{2} \left(1 + \frac{-4 + x_1}{\sqrt{-8x_1 + x_1^2 + 16(1 + x_2)}} \right),$$

$$\frac{\partial \sigma}{\partial x_2} = \frac{4}{\sqrt{-8x_1 + x_1^2 + 16(1 + x_2)}}.$$

Hence, $\frac{\partial \sigma}{\partial x_2} > 0$. Since $\sqrt{-8x_1 + x_1^2 + 16(1 + x_2)} > -4 + x_1$, we also obtain $\frac{\partial \sigma}{\partial x_1} > 0$.

Finally, when $x \in C_3$ the conclusion either follows from Lemma S.2 or from the monotonicity of $x_1 + 2x_2$. Q.E.D.

As noted in the main paper, we define $V : \Pi \rightarrow \mathbf{R}$ by $V(\pi) = h(\bar{x}^\pi, \underline{x}^\pi)$, where \underline{x}^π is the smallest point in the support of π and \bar{x}^π is the largest. Recall that h is defined on $\{(x_1, x_2) \in \mathbf{R}_+^2 : x_1 \geq x_2\}$. So the definition of V shows that the preferences represented by V are symmetric across a 45 degree line. Write $\pi < \pi'$ if π' strictly first-order stochastically dominates π . Let F_π and $F_{\pi'}$ be the cumulative distribution functions (CDFs) of π and π' , respectively.

LEMMA S.5: *The relationship $\pi < \pi'$ implies that $V(\pi) < V(\pi')$.*

PROOF: Assume $\pi < \pi'$. By Lemma S.4, it suffices to show that $\underline{x}^\pi \leq \underline{x}^{\pi'}$ and $\bar{x}^\pi \leq \bar{x}^{\pi'}$, and that at least one of the inequalities is strict. Suppose that $\underline{x}^\pi > \underline{x}^{\pi'}$ or $\bar{x}^\pi > \bar{x}^{\pi'}$. By choosing x such that $\underline{x}^{\pi'} < x < \min\{\bar{x}^{\pi'}, \underline{x}^\pi\}$, we have $F_{\pi'}(x) = 1/2 > 0 = F_\pi(x)$. This contradicts that $\pi < \pi'$. Hence, $\underline{x}^\pi \leq \underline{x}^{\pi'}$. In the same way, we obtain $\bar{x}^\pi \leq \bar{x}^{\pi'}$. Moreover, since $\pi \neq \pi'$, we obtain $\underline{x}^\pi < \underline{x}^{\pi'}$ or $\bar{x}^\pi < \bar{x}^{\pi'}$. Q.E.D.

For any $\pi \in \Pi$, let $e(\pi)$ be the degenerate lottery that yields the expected value of π (recall that π has finite support) with probability 1. The following result is immediate from Lemma S.3.

LEMMA S.6: *We have $V(\pi) \leq V(e(\pi))$.*

Lemma S.5 establishes that V represents probabilistically sophisticated preferences. Lemma S.6 says that the preferences are also risk-averse. We now proceed to verify that the data set defined at the outset is rationalizable an agent with utility function V . We write $\pi_x \in \Pi$ for the probability measure induced by $x \in \mathbf{R}_+^2$.

For observation 1, the budget set is

$$B(p^1, p^1 \cdot x^1) = \{x \in \mathbf{R}_+^2 : x_1 + 2x_2 \leq 6\}.$$

For all $x \in B(p^1, p^1 \cdot x^1)$, it is clear that $\max\{x_1, x_2\} + 2\min\{x_1, x_2\} \leq x_1 + 2x_2 \leq 6$ and, hence, that

$$V(\pi_x) = \frac{1}{3}(\max\{x_1, x_2\} + 2\min\{x_1, x_2\}) \leq 2 = V(\pi_{x^1}).$$

For observation 2, the budget set is

$$B(p^2, p^2 \cdot x^2) = \{x \in \mathbf{R}_+^2 : x_1 + x_2 \leq 8\}.$$

Note that $h(x) \leq 2$ for all $x \in C_3$ and $h(x) \leq 4$ for all $x \in C_2$. Since $B(p^2, p^2 \cdot x^2) \cap C_1$ consists of vectors for which $x_1 + x_2 = 8$ and since $h(x_1, x_2) = 4$ for those vectors, it follows that $V(\pi_x) \leq V(\pi_{x^2})$ for all $x \in B(p^2, p^2 \cdot x^2)$.

S.4. MAXMIN EXPECTED UTILITY

In this section, we provide the proof of Proposition 6. We restate Proposition 6.

PROPOSITION: *Let $S = K = 2$. Then a data set is maxmin expected utility rational if and only if it is SEU rational.*

PROOF: Let $(x^k, p^k)_{k=k_1, k_2}$ be a data set. Suppose that the data set is maxmin rational. Then there is a set

$$M = \{\lambda \underline{\mu} + (1 - \lambda) \bar{\mu} : \lambda \in [0, 1]\}$$

of probabilities for some $\underline{\mu}, \bar{\mu} \in \Delta_{++}$, and a strictly increasing and concave utility u satisfying the conditions stated above. Suppose without loss of generality that $\underline{\mu}_{s_1} < \bar{\mu}_{s_1}$.

Let

$$\mu^k \in \arg \min_{\mu \in M} \sum_{s \in S} \mu_s u(x_s^k) \quad \text{and} \quad v_s^k \in \partial u(x_s^k),$$

and let $\lambda^k > 0$ be such that $\mu_s^k v_s^k = \lambda^k p_s^k$ for all k and s .

Using the first-order conditions, we obtain

$$(S.1) \quad A = \frac{v_{s_1}^{k_1} v_{s_2}^{k_2}}{v_{s_2}^{k_1} v_{s_1}^{k_2}} = \left[\frac{\mu_{s_2}^{k_1}}{\mu_{s_1}^{k_1}} \frac{\mu_{s_1}^{k_2}}{\mu_{s_2}^{k_2}} \right] \left[\frac{p_{s_1}^{k_1} p_{s_2}^{k_2}}{p_{s_2}^{k_1} p_{s_1}^{k_2}} \right].$$

By the concavity of u , $A \leq 1$. There are three cases to consider.

First, let $x_{s_1}^{k_1} > x_{s_2}^{k_1}$ and $x_{s_2}^{k_2} > x_{s_1}^{k_2}$. Then $x_{s_1}^{k_1} > x_{s_2}^{k_1}$ implies that $\mu^{k_1} = \underline{\mu}$, and $x_{s_2}^{k_2} > x_{s_1}^{k_2}$ implies that $\mu^{k_2} = \bar{\mu}$. Then

$$\frac{\mu_{s_2}^{k_1}}{\mu_{s_1}^{k_1}} \frac{\mu_{s_1}^{k_2}}{\mu_{s_2}^{k_2}} = \frac{\bar{\mu}_{s_1}}{\underline{\mu}_{s_1}} \frac{\mu_{s_2}}{\bar{\mu}_{s_2}} \geq 1.$$

Thus, $A \leq 1$ implies that SARSEU is not violated.

In second place, let $x_{s_1}^{k_1} > x_{s_1}^{k_2}$, $x_{s_2}^{k_2} > x_{s_2}^{k_1}$, and $x_{s_1}^{k_1} > x_{s_2}^{k_1}$. Then $x_{s_1}^{k_1} > x_{s_2}^{k_1}$ implies that $\mu^{k_1} = \underline{\mu}$, and we have that

$$\frac{\mu_{s_2}^{k_1}}{\mu_{s_1}^{k_1}} \frac{\mu_{s_1}^{k_2}}{\mu_{s_2}^{k_2}} = \frac{\mu_{s_1}^{k_2}}{\underline{\mu}_{s_1}} \frac{\mu_{s_2}}{\mu_{s_2}^{k_2}} \geq 1,$$

as $\mu_{s_1}^{k_2} \geq \underline{\mu}_{s_1}$ and $\mu_{s_2} \geq \mu_{s_2}^{k_2}$. Thus, $A \leq 1$ implies that SARSEU is not violated.

Finally, let $x_{s_1}^{k_1} > x_{s_1}^{k_2}$, $x_{s_2}^{k_2} > x_{s_2}^{k_1}$, and $x_{s_1}^{k_1} \leq x_{s_2}^{k_1}$. Then

$$x_{s_2}^{k_2} > x_{s_2}^{k_1} \geq x_{s_1}^{k_1} > x_{s_1}^{k_2},$$

so $\mu^{k_2} = \bar{\mu}$. Thus,

$$\frac{\mu_{s_2}^{k_1} \mu_{s_1}^{k_2}}{\mu_{s_1}^{k_1} \mu_{s_2}^{k_2}} = \frac{\bar{\mu}_{s_1} \mu_{s_2}^{k_1}}{\mu_{s_1}^{k_1} \bar{\mu}_{s_2}} \geq 1,$$

as $\mu_{s_2}^{k_1} \geq \bar{\mu}_{s_2}$ and $\bar{\mu}_{s_1} \geq \mu_{s_1}^{k_1}$. Thus $A \leq 1$ implies that SARSEU is not violated. *Q.E.D.*

The result in the proposition does not, however, extend beyond the case of two observations. In the following discussion, we provide an example that (risk-averse) maxmin expected utility has testable implications beyond the (risk-averse) SEU model.

Assume $S = \{s_1, s_2\}$. Consider the consumption data set

	k_1	k_2	k_3	k_4
s_1	6	5	8	3
s_2	7	4	1	2

The table has x_s^k in entry (s, k) . We present a maxmin expected utility model that is a set M of probabilities and a concave utility u , such that the above consumptions are chosen for certain prices—the prices are defined below so that the relevant first-order conditions hold.

Let the set of probabilities be the convex hull of $\mu = (1 - q, q)$ and $\bar{\mu} = (q, 1 - q)$ with $q \in (1/2, 1)$. Denote this set of probabilities by M . Let $v(x) = \alpha - \beta x$ for $x \in [1/10, 10]$; define it in an arbitrary fashion outside of that interval, as long as it is strictly positive and decreasing. Then $u(x) = \int_0^x v(t) dt$ is a strictly monotone increasing and concave function.

Note that since u is strictly monotone increasing, $\min_{\mu \in M} \sum_{j=1,2} \mu_s u(x_{s_j}^{k_i}) = (1 - q)u(x_{s_1}^{k_i}) + qu(x_{s_2}^{k_i})$ for $i = 2, 3, 4$ and $\min_{\mu \in M} \sum_{j=1,2} \mu_s u(x_{s_j}^{k_1}) = qu(x_{s_1}^{k_1}) + (1 - q)u(x_{s_2}^{k_1})$. Note that the sequence $\{(x_{s_1}^{k_3}, x_{s_2}^{k_1}), (x_{s_1}^{k_1}, x_{s_2}^{k_2}), (x_{s_2}^{k_2}, x_{s_1}^{k_4}), (x_{s_2}^{k_4}, x_{s_1}^{k_3})\}$ satisfies properties (i), (ii), and (iii) in SARSEU.

Now let $p_{s_1}^{k_i} = (1 - q)v(x_{s_1}^{k_i})$ and $p_{s_2}^{k_i} = qv(x_{s_2}^{k_i})$ for $i = 2, 3, 4$. Let $p_{s_1}^{k_1} = qv(x_{s_1}^{k_1})$ and $p_{s_2}^{k_1} = (1 - q)v(x_{s_2}^{k_1})$. Then the maxmin expected utility defined by u and M satisfies the first-order conditions at the specified prices p^k and quantities x^k . We have that

$$\begin{aligned} \frac{p_{s_1}^{k_3} p_{s_1}^{k_1} p_{s_2}^{k_2} p_{s_2}^{k_4}}{p_{s_2}^{k_1} p_{s_1}^{k_2} p_{s_1}^{k_4} p_{s_2}^{k_3}} &= \frac{\alpha - \beta x_{s_1}^{k_3} \alpha - \beta x_{s_1}^{k_1} \alpha - \beta x_{s_2}^{k_2} \alpha - \beta x_{s_2}^{k_4}}{\alpha - \beta x_{s_2}^{k_1} \alpha - \beta x_{s_1}^{k_2} \alpha - \beta x_{s_1}^{k_4} \alpha - \beta x_{s_2}^{k_3}} \\ &\times \left(\frac{q}{1-q}\right) \left(\frac{q}{1-q}\right) \left(\frac{1-q}{q}\right) \left(\frac{q}{1-q}\right). \end{aligned}$$

Note that $(\frac{q}{1-q})(\frac{q}{1-q})(\frac{1-q}{q})(\frac{q}{1-q}) = (\frac{q}{1-q})^2 > 1$. By choosing α large enough, we obtain that $\frac{p_{s_1}^{k_3} p_{s_1}^{k_1} p_{s_2}^{k_2} p_{s_2}^{k_4}}{p_{s_2}^{k_1} p_{s_1}^{k_2} p_{s_1}^{k_4} p_{s_2}^{k_3}} > 1$. So SARSEU is violated.

S.5. OBSERVATIONAL EQUIVALENCE BETWEEN SEU AND SDU

In this section, we show that SEU and SDU are observationally equivalent under a particular condition on the data.

CONDITION S.7: There exists a permutation $s(1), s(2), \dots, s(|S|)$ of the set S of states such that for any $k, k' \in K$,

$$x_{s(t)}^k > x_{s(t')}^{k'} \Leftrightarrow t > t'.$$

Condition S.7 is plausible when prices and incomes do not vary much relative to beliefs. So across observations, the agent is likely to consume more in the states that she thinks are more likely.

PROPOSITION S.8: *Suppose that a data set $(x^k, p^k)_{k=1}^K$ satisfies Condition S.7. Then $(x^k, p^k)_{k=1}^K$ is SEU rational if and only if it is SDU rational.*

PROOF: Obviously, SEU rationality implies SDU rationality. To show the converse, suppose that the data set is SDU rational. Choose a sequence $\{(x_{s_i}^{k_i}, x_{s'_i}^{k'_i})\}_{i=1}^n$ such that (i) $x_{s_i}^{k_i} > x_{s'_i}^{k'_i}$ for all $i \in \{1, \dots, n\}$, (ii) each s appears as s_i the same number of times as s'_i , and (iii) each k appears as k_i the same number of times as k'_i .

Suppose that $s_i \neq s'_i$ for some i . Then by Condition S.7 there exist t, t' such that $t > t'$, and $s_i = s(t)$ and $s'_i = s(t')$. By (ii), then there must be $(x_{s_j}^{k_j}, x_{s'_j}^{k'_j})$ such that $s(t') = s_j$ and $s_j \neq s'_j$. Then, by Condition S.7 again, there must be t'' such that $t' > t''$ and $s(t'') = s'_j$. We can repeat this argument infinitely many times to find ever smaller t , which contradicts the finiteness of the set of states. Therefore, for each i , we have $s_i = s'_i$.

Hence, the $\{(x_{s_i}^{k_i}, x_{s'_i}^{k'_i})\}_{i=1}^n$ satisfies all of the conditions in SARSDU. Since the data set is SDU rational, Theorem 3 shows that

$$(S.2) \quad \prod_{i=1}^n \frac{p_{s_i}^{k_i}}{p_{s'_i}^{k'_i}} \leq 1.$$

Therefore, conditions (i), (ii), and (iii) imply (S.2), which is SARSEU. Hence, by Theorem 1, the data set must be SEU rational. *Q.E.D.*

S.6. OBJECTIVE EXPECTED UTILITY

In this section, we present the relationship between our main theorem and results in Green and Srivastava (1986), Varian (1983b), and Kubler, Selden, and Wei (2014). These authors discuss a setting where an objective probability $\mu \in \Delta_{++}$ is given. Given the objective probability μ , they seek to understand when there is a utility function for which the observed purchases maximize expected utility.

We show that we can write a version of our SARSEU that uses “risk-neutral” prices in place of regular prices. We show that this modified axiom characterizes the objective expected utility theory. Our modified SARSEU is, therefore, equivalent to the conditions studied by Green and Srivastava (1986) and Varian (1983b), and to the axiom in Kubler, Selden, and Wei (2014).

It is worth emphasizing that Kubler, Selden, and Wei (2014) allow μ to depend on k , so that the agent may use a different prior when faced with different optimization problems. In our subjective probability setup, this would make no sense because everything is rationalizable by suitably choosing priors in each optimization problem. Here we are being consistent with the rest of the paper in assuming a fixed prior through all observations, but the result can be relaxed to fit a variable-prior setup.

DEFINITION S.1: A data set $(x^k, p^k)_{k=1}^K$ is *objective expected utility (OEU) rational* if there is a concave and strictly increasing function $u : \mathbf{R}_+ \rightarrow \mathbf{R}$ such that, for all k ,

$$p^k \cdot y \leq p^k \cdot x^k \quad \Rightarrow \quad \sum_{s \in S} \mu_s u(y_s) \leq \sum_{s \in S} \mu_s u(x_s^k).$$

In the papers cited above, a crucial aspect of the data set is the price-probability ratios, or “risk-neutral prices,” defined as follows: for $k \in K$ and $s \in S$,

$$\rho_s^k = \frac{p_s^k}{\mu_s}.$$

A natural modification of SARSEU using the objective probability μ is the following.

STRONG AXIOM OF REVEALED OBJECTIVE EXPECTED UTILITY (SAROEU):
Assume any sequence of pairs $(x_{s_i}^{k_i}, x_{s_i}^{k'_i})_{i=1}^n$ in which the following statements hold:

- (i) We have $x_{s_i}^{k_i} > x_{s_i}^{k'_i}$ for all i .
- (ii) Each k appears in k_i (on the left of the pair) the same number of times it appears in k'_i (on the right):

The product of price-probability ratios satisfies that

$$\prod_{i=1}^n \frac{\rho_{s_i}^{k_i}}{\rho_{s'_i}^{k'_i}} \leq 1.$$

The prior μ is observable, so we do not need the requirement on s in SARSEU. Instead, SAROEU restricts the products of price-probability ratios, and not the product of price ratios.

The notion of data set in [Kubler, Selden, and Wei \(2014\)](#) is the same as in our paper. [Kubler, Selden, and Wei \(2014\)](#) investigate the case of strict concave utility, while we have focused on weak concavity. A modification of Kubler et al.'s axiom that allows for weak concavity is the following.¹

STRONG AXIOM OF REVEALED EXPECTED UTILITY (SAREU): For all $m \geq 1$ and sequences $k(1), \dots, k(m) \in K$,

$$\prod_{i=1}^m \left(\max_{s, s': x_s^{k(i)} > x_{s'}^{k(i+1)}} \frac{\rho_s^{k(i)}}{\rho_{s'}^{k(i+1)}} \right) \leq 1.$$

It is easy to modify the argument in [Kubler, Selden, and Wei \(2014\)](#) to show the equivalence of a data set being OEU rational, satisfying the conditions in [Green and Srivastava \(1986\)](#) and [Varian \(1983b\)](#).

PROPOSITION S.9: A data set is OEU rational if and only if it satisfies SAROEU.

This result implies that SAROEU, SAREU, and the conditions in [Green and Srivastava \(1986\)](#) and [Varian \(1983b\)](#) are equivalent.

PROOF OF PROPOSITION S.9: Using the result of [Kubler, Selden, and Wei \(2014\)](#), we prove the result by establishing the equivalence between SAROEU and SAREU.

Suppose that the data set $(x^k, p^k)_{k=1}^K$ satisfies SAROEU. Suppose, by way of contradiction, that SAREU is violated. Then there exist $m \geq 1$ and $k_1, \dots, k_m \in K$ such that $\prod_{i=1}^m (\max_{s, s': x_s^{k_i} > x_{s'}^{k_{i+1}}} (\rho_s^{k_i} / \rho_{s'}^{k_{i+1}})) > 1$. If $m = 1$, it clearly contradicts SAROEU.

¹SAREU and Kubler et al.'s axiom are different only in one point: their axiom requires

$$\prod_{i=1}^m (\max_{s, s': x_s^{k(i)} > x_{s'}^{k(i+1)}} \frac{\rho_s^{k(i)}}{\rho_{s'}^{k(i+1)}}) < 1.$$

In the following discussion, we will consider the case where $m > 1$. Then there exists a sequence $(x_{s_i}^{k_i^*}, x_{s_{i+1}'}^{k_{i+1}^*})_{i=1}^m$ with $k_{m+1}^* = k_1^*$ such that $\prod_{i=1}^m (\rho_{s_i}^{k_i^*} / \rho_{s_{i+1}'}^{k_{i+1}^*}) > 1$. Since the sequence satisfies the conditions in SAROEU, this contradicts SAROEU.

Now, we establish that SAREU implies SAROEU. Choose a sequence $(x_{s_i}^{k_i}, x_{s_{i+1}'}^{k_{i+1}'})_{i=1}^n$ of pairs in which $x_{s_i}^{k_i} > x_{s_{i+1}'}^{k_{i+1}'}$; each k appears in k_i (on the left of the pair) as many times as in k_{i+1}' (on the right). If $n = 1$, we have that $k_i = k_{i+1}' = k$. Consider the sequence $k(1) = k = k(2)$. Then SAREU implies that $\rho_s^k / \rho_{s'}^k \leq 1$, as desired.

Now, consider the case in which $n \geq 2$.

STEP 1: There exists a collection of cycles such that each cycle $(k(i))_{i=1}^{2m}$ satisfies (i) $x_{s(i)}^{k(i)} > x_{s'(i+1)}^{k(i+1)}$ for $i = 1, 3, \dots, 2m - 1$ and (ii) $k(2m) = k(1)$.

PROOF: First consider the pair $(x_{s_1}^{k_1}, x_{s_1'}^{k_1'})$. Let $k(1) = k_1$ and $k(2) = k_1'$. Since each k appears as k_i as many times as k_i' , there exists a pair $(x_{s_i}^{k_i}, x_{s_i'}^{k_i'})$ with $k_i = k(2)$. Let $k(3) = k_i$ and $k(4) = k_i'$. If $k(4) = k(1)$, then we have a cycle in k . Otherwise, for the same reason as was mentioned above, there is a $(x_{s_i}^{k_i}, x_{s_i'}^{k_i'})$ with $k_i = k(4)$. We can now let $k(5) = k_i$ and $k(6) = k_i'$. If $k(6) = k(1)$, then we again have a cycle. Since the number of data that appear in the sequence we started from is finite, we must eventually close a cycle. Each time we find a cycle, we can start the procedure from any remaining pair $(x_{s_i}^{k_i}, x_{s_i'}^{k_i'})$ in the data set. Since each k appears in k_i the same number of times it appears in k_i' , we must exhaust all pairs after finding a finite collection of cycles. *Q.E.D.*

STEP 2: We have $\prod_{i=1}^n \frac{\rho_{s_i}^{k_i}}{\rho_{s_i'}^{k_i'}} \leq 1$.

PROOF: For each cycle $(k(i))_{i=1}^{2m}$, we have that

$$\prod_{i=1}^{m/2} \frac{\rho_{s(2i-1)}^{k(2i-1)}}{\rho_{s'(2i)}^{k(2i)}} \leq \prod_{i=1}^{m/2} \left(\max_{s, s': x_s^{k(2i-1)} > x_{s'}^{k(2i)}} \left(\frac{\rho_s^{k(2i-1)}}{\rho_{s'}^{k(2i)}} \right) \right) \leq 1$$

as

$$\frac{\rho_{s(2i-1)}^{k(2i-1)}}{\rho_{s'(2i)}^{k(2i)}} \leq \max_{s, s': x_s^{k(2i-1)} > x_{s'}^{k(2i)}} \left(\frac{\rho_s^{k(2i-1)}}{\rho_{s'}^{k(2i)}} \right).$$

Then, since the product over each cycle does not exceed 1, the product of the cycles satisfies that

$$\prod_{i=1}^n \frac{\rho_{s_i}^{k_i}}{\rho_{s'_i}^{k'_i}} \leq 1.$$

Q.E.D.

S.7. GENERALIZATION: SUBJECTIVE-OBJECTIVE EXPECTED UTILITY

The purpose of this section is to lay out some details left out of Appendix B in the paper. Specifically, we allow that there are some states whose probabilities are objective and known to us. The set of state with known probabilities is $S^* \subseteq S$. The probability of a state s in S^* is μ_s^* . We allow for $S^* = S$ or $S^* = \emptyset$. Hence, the setup in this section contains as special cases the result in the previous section on objective expected utility and the main result in the paper on subjective expected utility.

Investigating the general case is important because since [Ellsberg \(1961\)](#), many experimenters test subjective expected utility theory in a setup where some states' probabilities are known. Indeed, in the experiments by [Ahn, Choi, Gale, and Kariv \(2014\)](#) and [Bossaerts, Ghirardato, Guarnaschelli, and Zame \(2010\)](#), the probability of one state is known and the probabilities of two other states are unknown. One can directly test the axiom presented here by using the experimental data obtained from [Ahn et al. \(2014\)](#) and [Bossaerts et al. \(2010\)](#). In those cases, since there is a single objective state, the presence of η (see Appendix B) means that the objective state is treated as subjective. As a consequence, if one rejects the axiom on such data, then the explanation cannot be that subjects doubt, or fail to understand, the experimenters' specification of objective uncertainty.

THEOREM S.10: *A data set is SOEU rational if and only if it satisfies SARSOEU.*

PROOF: The proof is similar to the proof of Theorem 1. Here, we outline the differences. Instead of Lemma 7, we can show that the following statements are equivalent:

- (i) We have that $(x^k, p^k)_{k=1}^K$ is SOEU rational.
- (ii) There are strictly positive numbers $(v_s^k)_{s \in S, k \in K}$, $(\lambda^k)_{k \in K}$, and $(\mu_s)_{s \in S \setminus S^*}$ such that

$$(S.3) \quad \begin{aligned} \mu_s v_s^k &= \lambda^k p_s^k & \text{if } s \notin S^*, \\ v_s^k &= \lambda^k \rho_s^k & \text{if } s \in S^*, \\ x_s^k > x_{s'}^{k'} &\Rightarrow v_s^k \leq v_{s'}^{k'}. \end{aligned}$$

Results similar to Lemmas 10, 12, and 13 continue to hold, with minor adaptations. There are no changes in Lemmas 8 and 9. As in Lemma 11, we need to prove that if $\log(r_s^k) \in \mathbf{Q}$ for all k and s , then there are numbers v_s^k , λ^k , and μ_s satisfying (S.3).

In the proof of the theorem, we need to change the definition of matrix A in two ways. Let A be a matrix with $K \times S$ rows and $K \times S + (S \setminus S^*) + K + 1$ columns, defined as follows: We have one row for every pair (k, s) , one column for every pair (k, s) , one column for every $s \in S \setminus S^*$, one column for each k , and one last column. Note the difference that the second column is now defined only for $s \in S \setminus S^*$.

In the row corresponding to (k, s) , the matrix has zeroes everywhere with the following exceptions: it has a 1 in the column for (k, s) , it has a 1 in the column for $s \in S \setminus S^*$, it has a -1 in the column for k , and it has $-\log r_s^k$ in the very last column, instead of $-\log p_s^k$.

The definitions of B and E are the same as in the proof of Lemma 11 with one difference: here, both B and E have 0 for each $s \in S \setminus S^*$, not for each $s \in S$. We can construct a sequence $(x_{s_i}^{k_i}, x_{s'_i}^{k'_i})_{i=1}^{n^*}$ of pairs that satisfies condition (i) in SARSOEU exactly as in Lemma 11.

The two differences in the definition of A lead to the two differences in the conclusion. First, since the second column is defined only for $s \in S \setminus S^*$, only for such s , we conclude that the number of times s appears as s_i equals the number of times it appears as s'_i . Therefore, condition (ii) in the axiom is satisfied. Condition (iii) holds as in Lemma 11.

Finally, we obtain

$$\prod_{i=1}^n \frac{r_{s_i}^{k_i}}{r_{s'_i}^{k'_i}} \leq 1$$

$$\text{instead of } \prod_{i=1}^n \frac{p_{s_i}^{k_i}}{p_{s'_i}^{k'_i}} \leq 1.$$

Q.E.D.

S.8. RELATIONSHIP BETWEEN SARSEU AND SAVAGE'S (1954) AXIOMS

In this section, we study the relationship between SARSEU and Savage's (1954) axioms. Savage's axiomatization involves seven axioms, labeled Axioms P1–P7. We show that SARSEU implies Savage's axioms, except for Axioms P1 and P6: Axiom P1 requires preference to be a weak order, which does not make sense for our primitive; Axiom P6 requires the set of states to be infinite.

Specifically, it is interesting to disentangle the role of SARSDU (Section 4 of the paper) and SARSEU in ruling out violations of Savage's axioms. It turns out that a violation of Axioms P2 or P7 will imply a violation of SARSDU,

the axiom behind a state-dependent representation. This makes sense, as Axioms P2 and P7 are essentially separability assumptions. A violation of Axiom P4 has a different structure, and we show that it violates SARSEU (actually it violates requirement (6)). Finally, Axioms P3 and P5 cannot be violated in our setup.

In this section, we use the following notations: For any $A \subset S$, and $x \in \mathbf{R}_+^S$ and $p \in \mathbf{R}_+^S$, x_A denotes the vector in \mathbf{R}_+^A obtained by restricting $s \mapsto x_s$ to A ; similarly, p_A denotes the vector in \mathbf{R}_+^A obtained by restricting $s \mapsto p_s$ to A .

Recall that Savage's primitive is a complete preference relation over acts. In contrast, our primitive is a data set $(x^k, p^k)_{k=1}^K$. To relate the two models, we define a revealed preference relation from the data set $(x^k, p^k)_{k=1}^K$ and investigate when it satisfies Savage's axioms.

DEFINITION S.2: For any $x, y \in \mathbf{R}_+^S$, the following statements hold:

- (i) We have $x \geq y$ if there exists $k \in K$ such that $x = x^k$ and $p^k \cdot x \geq p^k \cdot y$.
- (ii) We have $x > y$ if there exists $k \in K$ such that $x = x^k$ and $p^k \cdot x > p^k \cdot y$.²

There is one basic problem: Savage's primitive is a complete preference relation over acts, but a data set will contain much less information than a preference relation over \mathbf{R}_+^S . The revealed preference relation is going to be incomplete: many acts in \mathbf{R}_+^S will not be comparable. Such incompleteness gives rise to trivial violations of Savage's axioms, as his axioms were formulated for complete preferences. For example, one of Savage's axioms is as follows.

AXIOM P2: Let $x, y, x', y' \in \mathbf{R}_+^S$ and $A \subset S$ such that $x_A = x'_A$ and $y_A = y'_A$, and $x_{A^c} = y_{A^c}$ and $x'_{A^c} = y'_{A^c}$. Then $x \geq y$ if and only if $x' \geq y'$.

The revealed preference relation violates Axiom P2 when only one of x, y and x', y' is comparable. This is not a particularly interesting violation of Savage's axioms. A more meaningful exercise is to show how a violation of Savage's axioms that is not due to incompleteness implies a violation of SARSEU.

DEFINITION S.3: Let \geq be the revealed preference relation defined from $(x^k, p^k)_{k=1}^K$ by Definition S.2. Then we say that the data set violates Axiom P2 if there is $x, y, x', y' \in \mathbf{R}_+^S$ and $A \subset S$ as in the statement of Axiom P2 for which $x \geq y$ and $y' > x'$; or $y \geq x$ and $x' \geq y'$.

PROPOSITION S.11: If the data set violates Axiom P2, then it violates SARSDU.

PROOF: For a subset A of S and a data set $(x^k, p^k) \in \mathbf{R}_+^S \times \mathbf{R}_{++}^S$, we consider $(x_A^k, p_A^k) \in \mathbf{R}_+^A \times \mathbf{R}_{++}^A$. This defines a data set $(x_A^k, p_A^k)_{k=1}^K$ on a restricted domain with A (instead of S). On this restricted domain, we can define WARP

²It is worth emphasizing that this definition already has separability built in, which goes a long way to satisfying Savage's axioms.

and SARSDU in the same way as defined in Section 4. SARSDU implies WARP on this restricted domain.

Suppose that the data set $(x^k, p^k)_{k=1}^K$ violates Axiom P2. Then by definition of \succeq , and the fact that $x_{A^c} = y_{A^c}$ and $x'_{A^c} = y'_{A^c}$, the data set $(x^k_A, p^k_A)_{k=1}^K$ violates WARP. Then $(x^k_A, p^k_A)_{k=1}^K$ violates SARSDU, which implies that $(x^k, p^k)_{k=1}^K$ violates SARSDU. *Q.E.D.*

We shall use the following notation. We use 1_A to denote the indicator vector for $A \subset S$ in \mathbf{R}_+^S , and for a scalar $x \in \mathbf{R}_+$, $x1_A$ denotes the vector in \mathbf{R}_+^A with x in all its entries (the constant vector x).

AXIOM P4: *Suppose $A, B \subset S$; $x > y, x' > y'$. Then $(x1_A, y1_{A^c}) \succ (x1_B, y1_{B^c})$ if and only if $(x'1_A, y'1_{A^c}) \succ (x'1_B, y'1_{B^c})$.*

DEFINITION S.4: Let \succeq be the revealed preference relation defined from $(x^k, p^k)_{k=1}^K$ by Definition S.2. Then we say that the data set violates Axiom P4 if there is $A, B \subset S$ and scalars x, x', y, y' as in the statement of Axiom P4 for which $(x1_A, y1_{A^c}) \succ (x1_B, y1_{B^c})$ and $(x'1_B, y'1_{B^c}) \succeq (x'1_A, y'1_{A^c})$, or $(x1_B, y1_{B^c}) \succeq (x1_A, y1_{A^c})$ and $(x'1_A, y'1_{A^c}) \succ (x'1_B, y'1_{B^c})$.

PROPOSITION S.12: *If a data set violates Axiom P4, then it violates SARSEU.*

PROOF: Without loss of generality, we can assume that $\sum_{s \in S} p_s^k = 1$ for all k . The reason is that we can normalize prices to add up to 1 without affecting the validity of SARSEU.

Let $A, B \subset S$, and let x, x', y, y' be scalars as in the statement of Axiom P4, such that $(x1_A, y1_{A^c}) \succ (x1_B, y1_{B^c})$ and $(x'1_B, y'1_{B^c}) \succeq (x'1_A, y'1_{A^c})$. Suppose, toward a contradiction, that the data set satisfies SARSEU.

First, $(x1_A, y1_{A^c}) \succ (x1_B, y1_{B^c})$ means that there is an observation k for which $x^k = (x1_A, y1_{A^c})$ and

$$(S.4) \quad p^k \cdot x^k = p^k \cdot (x1_A, y1_{A^c}) > p^k \cdot (x1_B, y1_{B^c}),$$

while $(x'1_B, y'1_{B^c}) \succeq (x'1_A, y'1_{A^c})$ means that there is an observation k' such that

$$(S.5) \quad p^{k'} \cdot x^{k'} = p^{k'} \cdot (x'1_B, y'1_{B^c}) \geq p^{k'} \cdot (x'1_A, y'1_{A^c}).$$

Second, (S.4) implies that

$$x \sum_{s \in A} p_s^k + y \left(1 - \sum_{s \in A} p_s^k \right) > x \sum_{s \in B} p_s^k + y \left(1 - \sum_{s \in B} p_s^k \right)$$

and, therefore, that $\sum_{s \in A} p_s^k > \sum_{s \in B} p_s^k$, as $x > y$. Similarly, (S.5) and $x' > y'$ imply that $\sum_{s \in B} p_s^{k'} \geq \sum_{s \in A} p_s^{k'}$. Hence,

$$(S.6) \quad \sum_{s \in A \setminus B} p_s^k > \sum_{s \in B \setminus A} p_s^k \quad \text{and} \quad \sum_{s \in B \setminus A} p_s^{k'} \geq \sum_{s \in A \setminus B} p_s^{k'}.$$

Third, for any $s \in A \setminus B$ and any $s' \in B \setminus A$, we have that $x = x_s^k > x_{s'}^k = y$ and $x' = x_{s'}^{k'} > x_s^{k'} = y'$. Hence, SARSEU implies that

$$\frac{p_s^k p_{s'}^{k'}}{p_{s'}^k p_s^{k'}} \leq 1.^3$$

Thus, for any $s' \in B \setminus A$,

$$p_{s'}^{k'} \sum_{s \in A \setminus B} p_s^k \leq p_{s'}^k \sum_{s \in A \setminus B} p_s^{k'},$$

which implies that

$$\sum_{s' \in B \setminus A} p_{s'}^{k'} \sum_{s \in A \setminus B} p_s^k \leq \sum_{s' \in B \setminus A} p_{s'}^k \sum_{s \in A \setminus B} p_s^{k'},$$

a contradiction to (S.6). Q.E.D.

We now discuss Axioms P3 and P7 (Axiom P5 is a nontriviality axiom that is always satisfied in our setup). This requires some preliminary definitions.

DEFINITION S.5: For any $A \subset S$ and $x_A, y_A \in \mathbf{R}^A$, the following statements hold:

(i) We have $x_A \succeq_A y_A$ if there exist $z, w \in \mathbf{R}^S$ such that $z_A = x_A$ and $w_A = y_A$, and $z_{A^c} = w_{A^c}$, $z \succeq w$.

(ii) We have $x_A \succ_A y_A$ if there exist $z, w \in \mathbf{R}^S$ such that $z_A = x_A$ and $w_A = y_A$, and $z_{A^c} = w_{A^c}$, $z \succ w$.

DEFINITION S.6: The inclusion $A \subset S$ is *null* if for any $x, y \in \mathbf{R}_+^S$ such that $x_{A^c} = y_{A^c}$, it is false that $x \succ y$.

AXIOM P3: Suppose that A is not null. Then $x1_A \succ_A y1_A$ if and only if $x > y$.

AXIOM P7: We have that (i) $x_s 1_A \succ_A y_A$ for all $s \in A$ implies $x_A \succ_A y_A$; (ii) $y_A \succ_A x_s 1_A$ for all $s \in A$ implies $y_A \succ_A x_A$.

³Observe that here we are essentially using requirement (6).

DEFINITION S.7: Let \succeq be the revealed preference relation defined from $(x^k, p^k)_{k=1}^K$ by Definition S.2. Then we say that the data set violates the following statements:

1. It violates Axiom P3 if there is nonnull $A \subseteq S$, $x, y \in \mathbf{R}_+$, and $z \in \mathbf{R}_+^{A^c}$ for which $(x1_A, z) \succ (y1_A, z)$ and $y \geq x$, or $(y1_A, z) \succeq (x1_A, z)$ and $x > y$.
2. It violates Axiom P7 if there is a nonempty $A \subseteq S$ and $x, y \in \mathbf{R}_+^S$ such that one of the following statements is true:
 - (a) We have $y_A \succeq_A x_A$ while $x_s 1_A \succ_A y_A$ for all $s \in A$.
 - (b) We have $x_A \succeq_A y_A$ while $y_A \succ_A x_s 1_A$ for all $s \in A$.

PROPOSITION S.13: (i) No data set can violate Axiom P3. (ii) If a data set violates Axiom P7, then it violates SARSDU.

PROOF: Fix a data set that violates Axiom P3. Let A , x , y , and z be as in the definition of a violation of Axiom P3. Suppose that $(x1_A, z) \succ (y1_A, z)$ and $y \geq x$. Then there is an observation $x^k = (x1_A, z)$ with

$$\begin{aligned} x \sum_{s \in A} p_s^k + \sum_{s \in A^c} p_s^k z_s &= p^k \cdot (x1_A, z) > p^k \cdot (y1_A, z) \\ &= y \sum_{s \in A} p_s^k + \sum_{s \in A^c} p_s^k z_s. \end{aligned}$$

Hence, $x > y$, as $\sum_{s \in A} p_s^k > 0$. This contradicts that the data set violates Axiom P3.

Suppose that $y_A \succeq_A x_A$ while $x_s 1_A \succ_A y_A$ given A for all $s \in A$. Let k be such that $y_A = x_A^k$. For $s \in A$, let k_s be such that $x_s 1_A = x_A^{k_s}$. The inequality $y_A \succeq_A x_A$ implies $p_A^k \cdot x_A^k \geq p_A^k \cdot x_A$. For all $s \in A$, $x_s 1_A \succ_A y_A$ implies $p_A^{k_s} \cdot x_A^{k_s} > p_A^{k_s} \cdot x_A^k$.

Let s^* be such that $x_{s^*} \leq x_s$ for all $s \in A$. Then $p_A^k \cdot x_A^k \geq p_A^k \cdot x_A$ implies that $p_A^k \cdot x_A^k \geq p_A^k \cdot x_A^{k_{s^*}}$.

Now $p_A^{k_{s^*}} \cdot x_A^{k_{s^*}} > p_A^{k_{s^*}} \cdot x_A^k$ implies that the data set $(x_A^k, p_A^k)_{k=1}^K$ violates WARP on the restricted domain. So the data set $(x_A^k, p_A^k)_{k=1}^K$ must violate SARSDU on the restricted domain. Hence, the data set $(x_A^k, p_A^k)_{k=1}^K$ must violate SARSDU in the original domain. *Q.E.D.*

REFERENCES

- AFRIAT, S. N. (1967): "The Construction of Utility Functions From Expenditure Data," *International Economic Review*, 8 (1), 67–77. [2]
- AHN, D., S. CHOI, D. GALE, AND S. KARIV (2014): "Estimating Ambiguity Aversion in a Portfolio Choice Experiment," *Quantitative Economics*, 5 (2), 195–223. [17]
- BAYER, R.-C., S. BOSE, M. POLISSON, AND L. RENO (2012): "Ambiguity Revealed," Report, University of Adelaide. [1]
- BOSSAERTS, P., P. GHIRARDATO, S. GUARNASCHELLI, AND W. R. ZAME (2010): "Ambiguity in Asset Markets: Theory and Experiment," *Review of Financial Studies*, 23 (4), 1325–1359. [17]

- ELLSBERG, D. (1961): "Risk, Ambiguity, and the Savage Axioms," *Quarterly Journal of Economics*, 75, 643–669. [17]
- GREEN, R. C., AND S. SRIVASTAVA (1986): "Expected Utility Maximization and Demand Behavior," *Journal of Economic Theory*, 38 (2), 313–323. [14,15]
- KUBLER, F., L. SELDEN, AND X. WEI (2014): "Asset Demand Based Tests of Expected Utility Maximization," *American Economic Review*, 104 (11), 3459–3480. [14,15]
- SAVAGE, L. J. (1954): *The Foundations of Statistics*. New York: Wiley. [1,18]
- VARIAN, H. R. (1983a): "Nonparametric Tests of Consumer Behaviour," *Review of Economic Studies*, 50 (1), 99–110. [3]
- (1983b): "Nonparametric Tests of Models of Investor Behavior," *Journal of Financial and Quantitative Analysis*, 18 (3), 269–278. [14,15]

Caltech, 1200 E California Blvd., MC 228-77, Pasadena, CA 91125, U.S.A.;
fede@hss.caltech.edu

and

Caltech, 1200 E California Blvd., MC 228-77, Pasadena, CA 91125, U.S.A.;
saito@caltech.edu.

Manuscript received February, 2014; final revision received January, 2015.