THE UNIVERSITY OF CHICAGO
HARRIS SCHOOL
OF PUBLIC POLICY

MFS
MACRO FINANCE SOCIETY

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Monetary Policy and Asset Prices
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Problem set for Macro-Finance Society Summer School 2023

This problem set walks you through the replication code for "Why Does the Fed Move Markets so Much? A Model of Monetary Policy and Time-Varying Risk Aversion" (JFE, 2022) by Pflueger and Rinaldi. You are also asked to inspect the mechanism and produce additional comparative statics. You are encouraged to submit solutions by Monday August 22 to l.yepezsa95@gmail.com. Solutions will be available later.

1. Download the code and documentation from https://github.com/cpflueger/ProgrammingPackage_public/tree/main/ModelFOMCResponses
2. Run the file minimum_working_example_NK.m to replicate the main results from the paper.
3. How do the state variables respond to a monetary policy shock? Plot the impulse responses for the output gap, inflation, and policy rate, and surplus consumption rate between 0 and 16 quarters after a positive monetary policy surprise. Which state variable do you think is responsible for the persistent risk premium response to a monetary policy surprise in shown in the bottom-left panel in Figure 3?
    - Hint1: Impulse responses are saved in asset.Irf3
    - Hint2: You may want to num.Nsim=2 in line 274 and num.testirf=1 to switch off the simulations for the impulse responses and speed up the code.
4. How do the model results in Table 3 change when you increase the monetary policy output weight, γ^x, from 0.5 to 1? Explain.

Comments and questions regarding the beta version of the programming package are very welcome and should be submitted as issues to https://github.com/cpflueger/ProgrammingPackage_public