

Topics in Empirical Macroeconomics and Finance

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*“Chance favors only the prepared mind”.*¹ (Louis Pasteur, 1822-1895)

Lectures Tuesdays and Thursdays, 10:30-11:45am. Bunche Hall 9383.

Office hours Email me for an appointment.

Website <https://moodle2.sscnet.ucla.edu/course/view/18S-ECON221C-1>.

Grading First, I will ask you to replicate **two** empirical macro or/and finance papers, using **publicly available data** (e.g. national accounts, Compustat, CRSP, Nielsen Scanner data, other WRDS material, etc.), but for which the replication code was not made available online by the authors (or not fully). I shall give you a list of papers among which to choose at the very beginning of the quarter. See the preliminary timetable on page 15 for deadlines. I believe that the best way to learn empirical methods in macroeconomics and finance is to “get your hands dirty”, and practice working with data. The first replication exercise will count towards 40% of your final grade, and the second will count towards 40%. Second, I will ask you to **present a recent paper in empirical macroeconomics** during the last two lectures. (30 minutes each) Again, I will give you a list from which to choose. This will count towards 20% of your final grade.

Course outline This course will follow an inductive, or bottom-up, approach. Whenever possible, I will start from the facts, and review different theories in light of these facts. I will particularly emphasize empirical observations that have not been explained by currently discussed theories. My hope is that you will find here some inspiration for a dissertation topic. The course will constitute of four parts:

1. **Evidence-based macroeconomics (4 topics)** The first part of the course will introduce you to empirical methods in macroeconomics. We will discuss identification in macroeconomics through structural, narrative, and cross-sectional approaches; and compare the merits of these various approaches. These methods will be used throughout the rest of the class.

¹“La chance ne sourit qu’aux esprits bien préparés.”

2. **Consumption, Investment, the Trade Balance and Asset Pricing (5 topics)**
The second part of the class will be structured around empirical “puzzles”, which cannot be explained with neoclassical theories of consumption, investment, the trade balance and asset pricing (including exchange rates).
3. **Low interest rate macroeconomics (4 topics)** The third part will present evidence in favor of the “savings glut” hypothesis, and present overlapping-generations and some other models of “underconsumption”. I will also discuss issues of secular stagnation, competitiveness and external balance.
4. **Heterogeneity and macroeconomics (4 topics)** Finally, the last part of the course will focus on evidence and models of firm size and productivity heterogeneity, the labor income distribution, etc. I will finally cover some static optimal taxation.

Textbooks I will assume that you have basic knowledge of first year macroeconomics and finance, which can be found in many different textbooks. For macroeconomics, I would recommend:

- Romer, David. Advanced Macroeconomics. McGraw-Hill Education, 2011. [Link](#)
- Galí, Jordi. Monetary Policy, Inflation, and the Business Cycle: An Introduction to the New Keynesian Framework and Its Applications, Second Edition. Princeton University Press, 2015. [Link](#)
- Blanchard, Olivier Jean, and Stanley Fischer. Lectures on Macroeconomics. Vol. 12. 3. Cambridge, MA: The MIT Press, 1990. [Link](#)

If you are interested in how macroeconomics is used in practice, I strongly recommend:

- Bénassy-Quéré, Agnès, Benoît Coeuré, Pierre Jacquet, and Jean Pisani-Ferry. Economic Policy: Theory and Practice. Vol. 53. 9. Oxford, New York: Oxford University Press, 2013. [Link](#)

For finance, I would advise two excellent and complementary textbooks:

- Campbell, John Y. Financial Decisions and Markets: A Course in Asset Pricing. Princeton University Press, 2017. [Link](#)
- Cochrane, John H. Asset Pricing (Revised Edition). Princeton University Press, 2009. [Link](#)

Bibliography

Articles with a  symbol will be covered during class. The list of articles may change during the quarter.

Methodology

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Part I

Evidence-based macroeconomics

1 Causality in macroeconomics

Sims, Christopher A. “Macroeconomics and Reality.” *Econometrica* 48, no. 1 (1980): 1–48. [Link](#)

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Summer Institute Econometric Lecture, 2010, “Financial Econometrics”, Sydney Ludvigson, Yacine Ait-Sahalia, Michael Brandt, & Andrew Lo. [Link](#)

Angrist, Joshua D., and Jörn-Steffen Pischke. “The Credibility Revolution in Empirical Economics: How Better Research Design Is Taking the Con out of Econometrics.” *Journal of Economic Perspectives* 24, no. 2 (2010): 3–30. [Link](#)

Sims, Christopher A. “But Economics Is Not an Experimental Science.” *Journal of Economic Perspectives* 24, no. 2 (June 2010): 59–68. [Link](#)

Summer Institute Econometric Lecture, 2011, “Computational Tools & Macroeconomic Applications”, Lawrence Christiano and Jesus Fernandez-Villaverde. [Link](#)

📖 “Empirical Macroeconomics. Thomas J. Sargent and Christopher A. Sims” Scientific Background on the Sveriges Riksbank Prize in Economic Sciences in Memory of Alfred Nobel 2011. [Link](#)

📖 Uhlig, Harald. “Economics and Reality.” *Journal of Macroeconomics*, Has macro progressed?, 34, no. 1 (March 1, 2012): 29–41. [Link](#)

☞ Ramey, V. A. “Chapter 2 - Macroeconomic Shocks and Their Propagation.” In *Handbook of Macroeconomics*, edited by John B. Taylor and Harald Uhlig, 2:71–162. Elsevier, 2016. [Link](#)

☞ Nakamura, Emi, and Jón Steinsson. “Identification in Macroeconomics.” Working Paper. National Bureau of Economic Research, October 2017. [Link](#)

2 Model-based identification / Structural VARs

Summers, Lawrence H. “Some Skeptical Observations on Real Business Cycle Theory.” *Minneapolis Quarterly Review*, no. Fall (1986): 23–27. [Link](#)

Prescott, Edward C. “Response to a Skeptic.” *Minneapolis Quarterly Review*, no. Fall (1986): 28. [Link](#)

Blanchard, Olivier Jean, and Danny Quah. “The Dynamic Effects of Aggregate Demand and Supply Disturbances.” *The American Economic Review* 79, no. 4 (1989): 655–73. [Link](#)

Summers, Lawrence H. “The Scientific Illusion in Empirical Macroeconomics.” *The Scandinavian Journal of Economics* 93, no. 2 (1991): 129–48. [Link](#)

☞ Hansen, Lars Peter, and James J. Heckman. “The Empirical Foundations of Calibration.” *Journal of Economic Perspectives* 10, no. 1 (March 1996): 87–104. [Link](#)

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Galí, Jordi, and Pau Rabanal. “Technology Shocks and Aggregate Fluctuations: How Well Does the Real Business Cycle Model Fit Postwar U.S. Data?” In *NBER Macroeconomics Annual* 2004, 19:1–25. April, 2005. [Link](#)

☞ Uhlig, Harald. “What Are the Effects of Monetary Policy on Output? Results from an Agnostic Identification Procedure.” *Journal of Monetary Economics* 52, no. 2 (March 1, 2005): 381–419. [Link](#)

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Velde, François R. “Chronicle of a Deflation Unforetold.” *Journal of Political Economy* 117, no. 4 (August 1, 2009): 591–634. [Link](#)

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Mertens, Karel, and Morten O. Ravn. “Empirical Evidence on the Aggregate Effects of Anticipated and Unanticipated US Tax Policy Shocks.” *American Economic Journal: Economic Policy* 4, no. 2 (May 2012): 145–81. [Link](#)

☞ Cloyne, James. “Discretionary Tax Changes and the Macroeconomy: New Narrative Evidence from the United Kingdom.” *American Economic Review* 103, no. 4 (June 2013): 1507–28. [Link](#)

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☞ Gertler, Mark, and Peter Karadi. “Monetary Policy Surprises, Credit Costs, and Economic Activity.” *American Economic Journal: Macroeconomics* 7, no. 1 (January 2015): 44–76. [Link](#)

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Part II

Consumption, Investment, Asset Pricing and the Trade Balance

5 Investment: benchmark and puzzles

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Summers, Lawrence H., Barry P. Bosworth, James Tobin, and Philip M. White. “Taxation and Corporate Investment: A Q-Theory Approach.” *Brookings Papers on Economic Activity* 1981, no. 1 (1981): 67–140. [Link](#)

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6 Asset pricing: benchmark and puzzles

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7 Investment and financial frictions

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8 Asset pricing and financial frictions

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Part III

Low interest rates macroeconomics

10 The New Keynesian Model and the Liquidity Trap

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12 OLG models, public debt, rational bubbles

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13 Low interest rates: demand or supply

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Part IV

Heterogeneity and macro

15 Size / wage distributions: evidence

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17 Size / wage distributions: assignment models

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18 Static optimal taxation

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Tentative Course Time Table - Spring 2018

I - Evidence-based macroeconomics

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|---|----------------|
| 1. Causality in macroeconomics | April 3, 2018 |
| 2. Model-based identification / Structural VARs | April 5, 2018 |
| 3. Narrative approach and case/event studies | April 10, 2018 |
| 4. Cross-sectional data and model based aggregation | April 12, 2018 |
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II - Consumption, Investment, Asset Pricing and the Trade Balance

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|--|-----------------------|
| 5. Investment: benchmark and puzzles | April 17, 2018 |
| 6. Asset pricing: benchmark and puzzles | April 19, 2018 |
| 7. Investment and financial frictions | April 24, 2018 |
| 8. Asset pricing and financial frictions | April 26, 2018 |
| Replication 1 proposal due | April 29, 2018 |
| 9. Behavioral asset pricing | May 1, 2018 |
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III - Low interest rates macroeconomics

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|--|---------------------|
| 10. The New Keynesian Model and the Liquidity Trap | May 3, 2018 |
| 11. Measuring the marginal product of capital | May 8, 2018 |
| 12. OLG models, public debt, rational bubbles | May 10, 2018 |
| Replication 1 due | May 13, 2018 |
| 13. Low interest rates: demand or supply | May 15, 2018 |
| 14. External balance and competitiveness | May 17, 2018 |
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IV - Heterogeneity and macro

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|--|---------------------|
| 15. Size / wage distributions: evidence | May 22, 2018 |
| 16. Size / wage distributions: dynamic theories | May 24, 2018 |
| Presentation / Replication 2 proposal due | May 27, 2018 |
| 17. Size / wage distributions: assignment models | May 29, 2018 |
| 18. Static optimal taxation | May 31, 2018 |
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Presentations	June 5/7, 2018
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Replication 2 due	June 8, 2018
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