



*E*conometrics of *H*uman *C*apital

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Parameters of Interest

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Heckman (2008) sets out three tasks for us:

- ▶ Defining the Set of Hypotheticals or Counterfactuals
⇒ A Scientific Theory
- ▶ Identifying Causal Parameters from Hypothetical Population Data
⇒ Mathematical Analysis of Data Point or Set Identification
- ▶ Identifying Parameters from Real Data
⇒ Estimation and Testing Theory

Parameters of Interest

- ▶ conventional average effects
- ▶ policy-relevant average effects
- ▶ marginal effects
- ▶ distributional effects
- ▶ effects on distributions

Setup

The Generalized Roy Model

Potential Outcomes

$$Y_1 = \mu_1(X) + U_1$$

$$Y_0 = \mu_0(X) + U_0$$

Observed Outcome

$$Y = DY_1 + (1 - D)Y_0$$

Choice

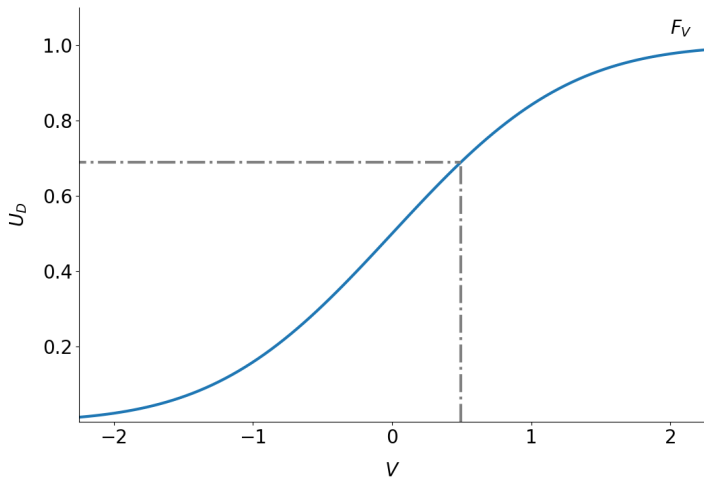
$$D = I[\mu_D(X, Z) - V > 0]$$

Useful Notation

$$P(X, Z) = \Pr(D = 1 \mid X, Z) = F_V(\mu_D(X, Z))$$

$$U_D = F_V(V)$$

Figure: First-state unobservable



Individual Heterogeneity

Individual-specific Benefit of Treatment

$$Y_1 - Y_0 = (\mu_1(X) - \mu_0(X)) + (U_1 - U_0)$$

Sources of Heterogeneity

- ▶ Difference in Observable Characteristics
- ▶ Difference in Unobservable Characteristics
 - ▶ Uncertainty
 - ▶ Private Information

Figure: Distribution of Benefits



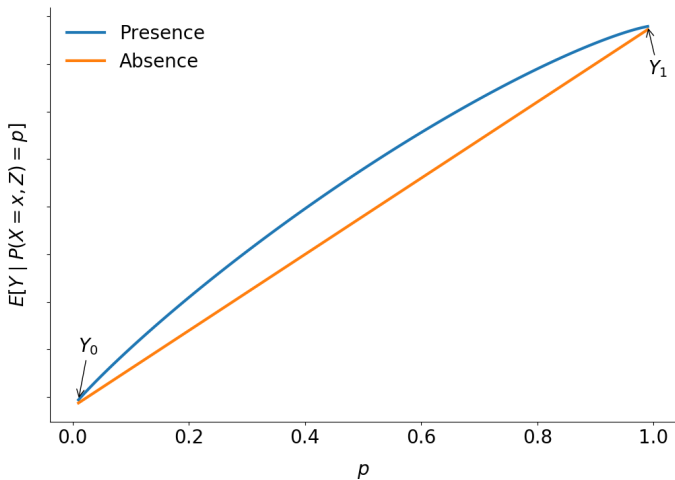
Essential Heterogeneity

Definition: Individuals select their treatment status based on gains unobservable by the econometrician. More formally,

$$Y_1 - Y_0 \not\perp D \mid X = x.$$

⇒ consequences for the estimation strategy

Figure: Conditional Expectation and Essential Heterogeneity



Conventional Average Treatment Effects

Conventional Average Treatment Effects

$$B^{ATE} = E[Y_1 - Y_0]$$

$$B^{TT} = E[Y_1 - Y_0 \mid D = 1]$$

$$B^{TUT} = E[Y_1 - Y_0 \mid D = 0]$$

⇒ correspond to *extreme* policy alternatives

Selection Problem

$$\begin{aligned} E[Y \mid D = 1] - E[Y \mid D = 0] &= \underbrace{E[Y_1 - Y_0]}_{B^{ATE}} \\ &+ \underbrace{E[Y_1 - Y_0 \mid D = 1] - E[Y_1 - Y_0]}_{\text{Selection on gains}} \\ &+ \underbrace{E[Y_0 \mid D = 1] - E[Y_0 \mid D = 0]}_{\text{Selection on levels}} \end{aligned}$$

$$\begin{aligned}
 E[Y \mid D = 1] - E[Y \mid D = 0] &= \underbrace{E[Y_1 - Y_0 \mid D = 1]}_{B^{TT}} \\
 &\quad + \underbrace{E[Y_0 \mid D = 1] - E[Y_0 \mid D = 0]}_{\text{Selection on levels}}
 \end{aligned}$$

⇒ the bias depends on the parameter of interest

Figure: Distribution of Effects with Essential Heterogeneity

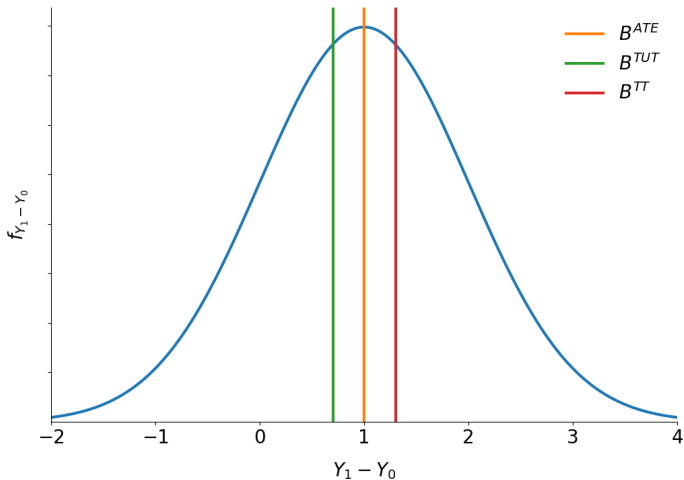
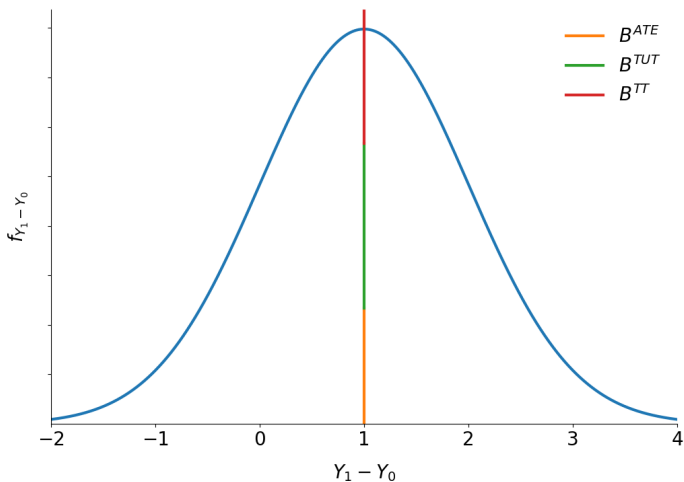


Figure: Distribution of Effects without Essential Heterogeneity



Policy-Relevant Average Treatment Effects

Observed Outcomes

$$Y_B = D_B Y_1 + (1 - D_B) Y_0$$

$$Y_A = D_A Y_1 + (1 - D_A) Y_0$$

Effect of Policy

$$B^{PRTE} = \frac{1}{E[D_A] - E[D_B]} (E[Y_A] - E[Y_B])$$

Marginal Effect of Treatment

Marginal Benefit of Treatment

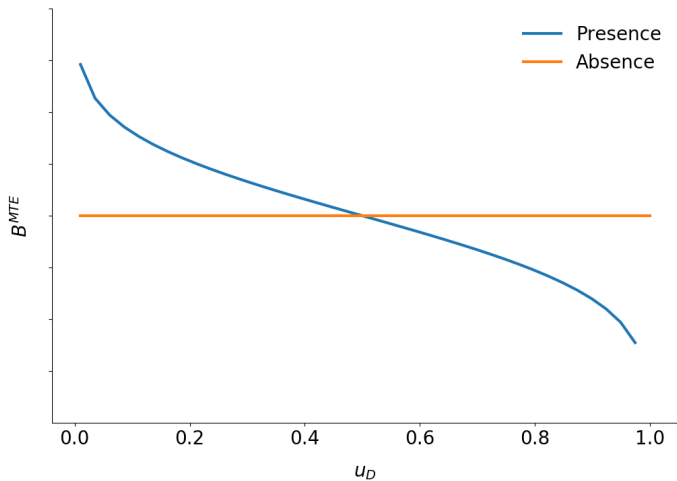
$$B^{MTE}(x, u_D) = E[Y_1 - Y_0 \mid X = x, U_D = u_D]$$

Intuition: Mean gross return to treatment for persons at quantile u_D of the first-stage unobservable V

Figure: Margin of Indifference



Figure: Marginal Benefit of Treatment



Effects of Treatment as Weighted Averages Parameter Δ_j , can be written as a weighted average of the $B^{MTE}(x, u_D)$.

$$\Delta_j(x) = \int_0^1 B^{MTE}(x, u_D) \omega^j(x, u_D) du_D,$$

where the weights $\omega^j(x, u_D)$ are specific to parameter j and integrate to one.

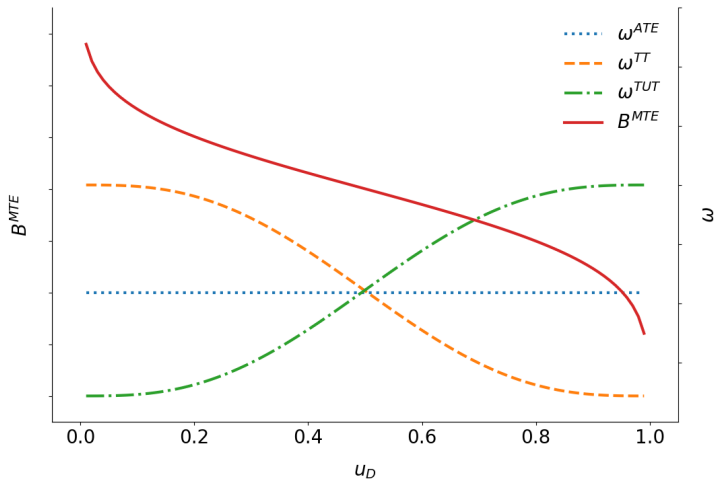
Weights

$$\omega^{ATE}(x, u_D) = 1$$

$$\omega^{TT}(x, u_D) = \frac{1 - F_{P|X=x}(u_D)}{E[P \mid X = x]}$$

$$\omega^{TUT}(x, u_D) = \frac{F_{P|X=x}(u_D)}{E[1 - P \mid X = x]}$$

Figure: Effects of Treatment as Weighted Averages



Local Average Treatment Effect

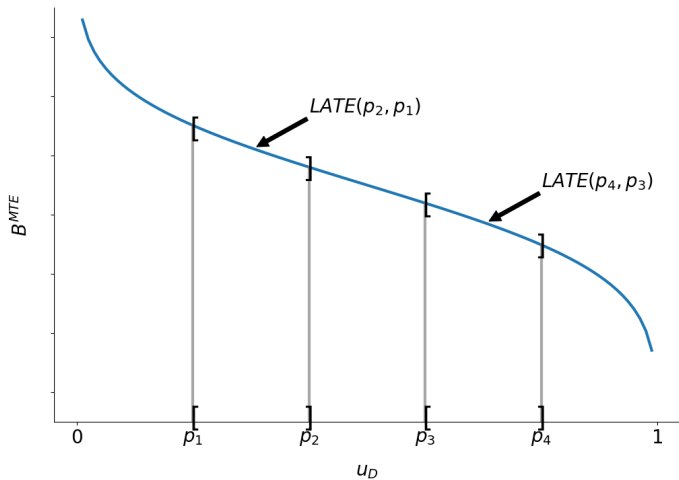
Local Average Treatment Effect

- ▶ **Local Average Treatment Effect:** Average effect for those induced to change treatment because of a change in the instrument.
⇒ instrument-dependent parameter
- ▶ **Marginal Treatment Effect:** Average effect for those individuals with a given unobserved desire to receive treatment.
⇒ deep economic parameter

$$B^{LATE} = \frac{E(Y | Z = z) - E[Y | Z = z']}{P(z) - P(z')}$$

$$B^{LATE}(x, u_D, u_{S'}) = \frac{1}{u_D - u_{D'}} \int_{u_D}^{u_{S'}} B^{MTE}(x, u) du,$$

Figure: Local Average Treatment Effect



Distributions of Effects

Figure: Distribution of Potential Outcomes

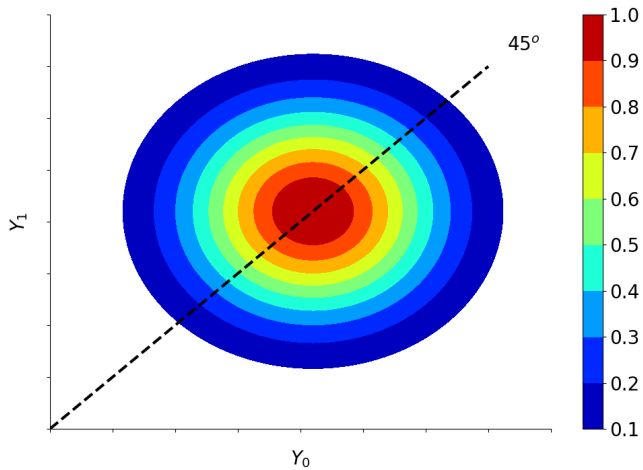
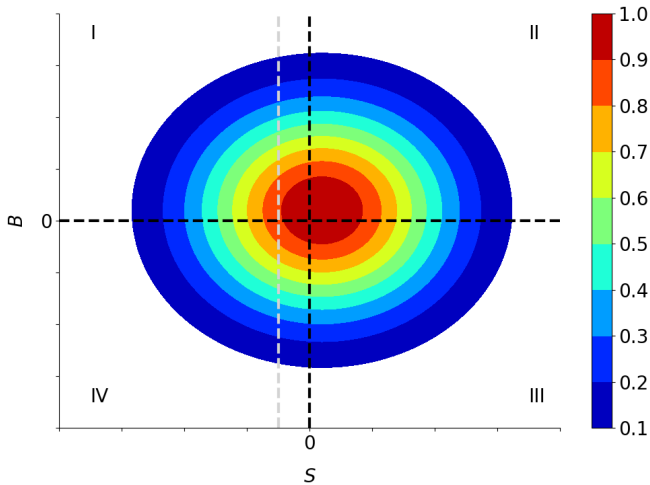


Figure: Distribution of Benefits and Surplus



Appendix

References

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