

Macroeconomic Theory II: Syllabus

In the second semester of the macroeconomic theory sequence we will use the tools developed before to study general equilibrium models with heterogeneous agents. We will analyze optimal fiscal and monetary government policies, models useful for analyzing the effects of social security reforms, equilibrium search, optimal contracts and credit market frictions. In order to better understand the models, we will also use computer simulations in Matlab.

The grade distribution will be based on problem sets, midterm and final. Policies related to student conduct will be strictly enforced.

Topics

Papers with * will be covered in class.

General equilibrium with heterogeneous agents Cooley (1995, Chapter 4) and Ljungquist and Sargent (Chapter 13 and 14), and Ljungquist and Sargent 2nd edition (Chapter 17), Ventura (1999)*, Conesa and Krueger (1999)*, Imrohorglu (1992)*, Krusell and Smith (1998)*, Aiyagari (1994b), Aiyagari (1994a) Sargent (1999), Diaz-Gimenez, Prescott, Fitzgerald, and Alvarez (1992), Huggett (1993), Huggett (1996), Huggett (1997), Huggett and Ventura (1999), Lucas (1980), Lucas (1992).

Equilibrium search Lucas and Prescott (1974)* and its version in Stokey, Lucas, and Prescott (1989) in Chapter 13, Alvarez and Veracierto (1999a)*, Alvarez and Veracierto (1999b), Veracierto (2001), Lagos (2001). Sargent (1987) and Sargent and Ljungquist (2000) provide a good survey of search.

Asymmetric Information and Optimal Contracts Mas-Collel *etal.* (Chapter 14, 1995), Marcet and Marimon (1999), Hansen and Imrohorglu (1992), Cooley, Marimon, and Quadrini (2001), Cooley and Quadrini (1999), Rogerson (1985), Clementi and Hopenhayn (2002), Phelan and Townsend (1991), Atkeson and Lucas (1992), Atkeson and Lucas (1995).

Capacity constraints and politico-economic equilibrium Cooley, Hansen, and Prescott (1995), Hansen and Prescott (1998), Klein and Rios-Rull (2004)*, and Krusell, Quadrini, and Rios-Rull (1997)*.

Credit markets and frictions Kiyotaki and Moore (1997), Kiyotaki and Moore (2001), Fuerst (1995), Smith and Wang (2000), Gertler (1988), Gertler and Gilchrist (1994), Gentry and Hubbard (2000), Lucas (1978), Bernanke and Gertler (1989), Williamson (1987), Kehoe and Levine (1993), King and Levine (1993), Levine (1997), Jermann and Quadrini (2003), Gomes (2001), Fuerst (1992), Fazzari, Hubbard, and Petersen (1988), Quadrini (1999), Diaz-Gimenez, Prescott, Fitzgerald, and Alvarez (1992),

Textbooks

Cooley, Thomas F., Editor. *Frontiers of Business Cycle Research*. Princeton University Press: 1995.

- Ljungquist, Lars, and Thomas J. Sargent. *Recursive Macroeconomic Theory*. MIT Press, 2000, and Chicago: Manuscript, University of Chicago, 1999.
- Lucas, Robert E., Jr. *Studies in the Business Cycle Theory*. Cambridge: MIT Press, 1984.
- Lucas, Robert E., Jr. *Models in Business Cycles*. Yrjo Jahnsson Lectures Series. London: Blackwell, 1987.
- Romer Paul. *Advanced Macroeconomics*. McGraw-Hill: 1996.
- Sargent, Thomas J. *Dynamic Macroeconomic Theory*. Cambridge: Harvard University Press, 1987.
- Stokey, Nancy L., Robert E. Lucas, Jr., and Edward C. Prescott. *Recursive Methods in Economic Dynamics*. Cambridge: Harvard University Press, 1989.

Reading List

- Aiyagari, R. S. (1994a). Macroeconomics with frictions. *Federal Reserve Bank of Minneapolis Staff Report 18(3)*, 24–40.
- Aiyagari, R. S. (1994b). Uninsured idiosyncratic risk and aggregate savings. *Quarterly Journal of Economics 109(3)*, 659–684.
- Alvarez, F. and M. Veracierto (1999a). Labor market policies in an equilibrium search model. *NBER Macroeconomic Annual (14)*, 265–304.
- Alvarez, F. and M. Veracierto (1999b). Severance payments in an economy with frictions. *Journal of Monetary Economics (47)*, 477–498.
- Atkeson, A. and R. E. Lucas, Jr. (1992). On efficient distribution with private information. *Review of Economic Studies 59*, 427–453.
- Atkeson, A. and R. E. Lucas, Jr. (1995). Efficiency and equality in a simple model of efficient unemployment insurance. *Journal of Economic Theory 66*, 64–98.
- Bernanke, B. S. and M. Gertler (1989). Agency cost, net worth and business fluctuations. *American Economic Review 79(1)*, 14–31.
- Clementi, G. L. and H. A. Hopenhayn (2002). A theory of financing constraints and firm dynamics. *Working paper*.
- Conesa, J. C. and D. Krueger (1999). Social security reform with heterogeneous agents. *Review of Economic Dynamics 2(4)*, 757–795.
- Cooley, T. F., G. D. Hansen, and E. C. Prescott (1995). Equilibrium business cycles with idle resources and variable capacity utilization. *Economic Theory 6*, 35–49.
- Cooley, T. F., R. Marimon, and V. Quadrini (2001). Aggregate consequences of limited contract enforceability. *Unpublished manuscript*.
- Cooley, T. F. and V. Quadrini (1999). Monetary policy and the financial decision of firms. *Unpublished manuscript*.
- Diaz-Gimenez, J., E. C. Prescott, T. Fitzgerald, and F. Alvarez (1992). Banking in computable general equilibrium economies. *Journal of Economic Dynamics and Control 16*, 533–559.

- Fazzari, S. M., G. R. Hubbard, and B. C. Petersen (1988). Financing constraint and corporate investment. *Brookings Papers on Economic Activity* (1), 141–195.
- Fuerst, T. S. (1992). Liquidity, loanable funds, and real activity. *Journal of Monetary Economics* 29, 3–24.
- Fuerst, T. S. (1995). Monetary and financial interactions in the business cycle. *Journal of Money, Credit, and Banking* 27(4), 1319–1341.
- Gentry, W. and G. Hubbard (2000). Entrepreneurship and household savings. *Unpublished manuscript*.
- Gertler, M. (1988). Financial structure and aggregate economic activity: An overview. *Journal of Money, Credit and Banking* 20(3), 559–589.
- Gertler, M. and S. Gilchrist (1994). Monetary policy, business cycles, and the behavior of small manufacturing firms. *Quarterly Journal of Economics* CIX(2), 309–340.
- Gomes, J. (2001). Financing investment. *American Economic Review* 91(5), 1264–1285.
- Hansen, G. D. and A. Imrohoroglu (1992). The role of unemployment insurance in an economy with liquidity constraint and moral hazard. *Journal of Political Economy* 100(1), 118–142.
- Hansen, G. D. and E. C. Prescott (1998). Capacity constraints, asymmetries and the business cycle. *University of Chicago Working Paper*.
- Huggett, M. (1993). The risk-free rate in heterogeneous-agent incomplete-insurance economies. *Journal of Economic Dynamics and Control* 17, 953–969.
- Huggett, M. (1996). Wealth distribution in life-cycle economies. *Journal of Monetary Economics* 38, 469–494.
- Huggett, M. (1997). The one-sector growth model with idiosyncratic shocks: Steady states and dynamics. *Journal of Monetary Economics* 39, 385–403.
- Huggett, M. and G. Ventura (1999). On the distributional effects of social security reform. *Review of Economic Dynamics* 2, 498–531.
- Imrohoroglu, A. (1992). The welfare cost of inflation under imperfect insurance. *Journal of Economic Dynamics and Control* 16, 79–91.
- Jermann, U. and V. Quadrini (2003). Stock market boom and the productivity gains of the 1990s. *Manuscript*.
- Kehoe, T. J. and D. K. Levine (1993). Debt-constrained asset market. *Review of Economic Studies* 60, 865–888.
- King, R. G. and R. Levine (1993). Finance, entrepreneurship, and growth: Theory and evidence. *Journal of Monetary Economics* 32(3), 513–542.
- Kiyotaki, N. and J. Moore (1997). Credit cycles. *Journal of Political Economy* 105(2), 211–48.
- Kiyotaki, N. and J. Moore (2001). Liquidity, business cycles, and monetary policy. *Manuscript*.
- Klein, P. and J.-V. Rios-Rull (2004). Time-consistent optimal fiscal policy. *International Economic Review* 44(4), 1217–1245.
- Krusell, P., V. Quadrini, and J.-V. Rios-Rull (1997). Politico-economic equilibrium and economic growth. *Journal of Economic Dynamics and Control* 21, 243–272.
- Krusell, P. and A. A. J. Smith (1998). Income and wealth heterogeneity in the macroeconomy. *Journal of Political Economy* 106(5), 867–896.

- Lagos, R. (2001). An alternative approach to search frictions. *Journal of Political Economy* 108(5), 851–873.
- Levine, R. (1997). Financial development and economic growth: Views and agenda. *Journal of Economic Literature* 35(2), 688–726.
- Lucas, Jr., R. E. (1978). On the size distribution of business firms. *Bell Journal of Economics* 9, 508–523.
- Lucas, Jr., R. E. (1980). Equilibrium in a pure currency economy. *Economic Inquiry* 43, 203–220.
- Lucas, Jr., R. E. (1992). On efficiency and distribution. *The Economic Journal* (102), 233–247.
- Lucas, Jr., R. E. and E. C. Prescott (1974). Equilibrium search and unemployment. *Journal of Economic Theory* 7, 188–209.
- Marcet, A. and R. Marimon (1999). Recursive contracts. *Unpublished manuscript*.
- Phelan, C. and R. M. Townsend (1991). Computing multi-period, information-constrained optima. *Review of Economic Studies* 58, 853–881.
- Quadrini, V. (1999). Entrepreneurship, saving and social mobility. *Unpublished manuscript*.
- Rogerson, W. P. (1985). The first-order approach to principal-agent problems. *53*(6), 1357–1368.
- Sargent, T. J. (1999). Bewley models. *University of Chicago Manuscript*, Chapter 4, 49–71.
- Smith, Anthony A., J. and C. Wang (2000). Dynamic credit relationships in general equilibrium. *Unpublished manuscript*.
- Stokey, N. L., R. E. Lucas, Jr., and E. C. Prescott (1989). *Recursive Methods in Economic Dynamics*. Cambridge: Harvard University Press.
- Ventura, G. (1999). Flat tax reform: A quantitative exploration. *Journal of Economic Dynamics and Control* 23, 1425–1458.
- Veracierto, M. (2001). Employment flows, capital mobility, and policy analysis. *International Economic Review* 42(3), 571–595.
- Williamson, S. D. (1987). Financial intermediation, business failures, and real business cycles. *Journal of Political Economy* 95(6), 1196–1216.