

Economics 210Ca: Macroeconomics  
Spring 2012

Professor Marjorie Flavin

lectures: Tuesday and Thursday, 12:30 – 1:50, room 300

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office hours: TBD

TA: Myungkyu Shim

office hours: TBD

TA session: proposed for noon – 1:00 pm on Fridays

Econ 210C consists of two independent components, with this course, 210Ca taking the first five weeks of the quarter and the second component, Econ 210Cb, taught by Irina Telyukova, taking the last 5 weeks of the quarter. The in-class exam on Thursday, May 3 will be 80 minutes in length and will serve as the final for the 210Ca component. Your course grade for 210C as a whole will be the average of your grades on the two components.

Problem sets will be assigned weekly, and will be due in class on Tuesdays. Myungkyu will grade the problem sets and go over the solutions in his weekly TA session on Fridays. Your average for the set of problem sets will count as 20% of your grade for 210Ba. Collaborating on the problem sets is permitted; free-riding on the problem sets is discouraged.

Texts:

(LS) Ljungqvist and Sargent, *Recursive Macroeconomic Theory*, MIT Press, 2004

(AD) Angus Deaton, *Understanding Consumption*, Oxford University Press, 1992

(BF) Blanchard and Fischer, *Lectures in Macroeconomics*, MIT Press, 1989

**Schedule of lectures and related reading**

- Tuesday, April 3: Equilibrium consumption allocation under complete markets;  
Arrow-Debreu market structure; trades occur at time zero  
LS Sections 8.1-8.7
- Thursday, April 5: Equilibrium consumption allocation under complete markets;  
sequential trading with one-period Arrow securities  
LS Sections 8.8-8.10, 8.13, 8.18
- Tuesday, April 10: Euler equations  
with certainty equivalence (permanent income model)  
without certainty equivalence (general model)  
LS Sections 13.1-13.3  
Deaton, Chapter 1,3, and 4  
Hall, Robert, "Stochastic Implications of the Life Cycle Permanent  
Income Hypothesis: Theory and Evidence" JPE, 86 (Dec 1978),  
971-987.
- Thursday, April 12: Consumption-beta model  
LS Sections 13.4-13.9  
Lucas (1978), "Asset Prices in an Exchange Economy,  
Econometrica, 46, 6 (Dec), 1426-1445.  
Blanchard and Fischer, pp 279-291 and 506-512

- Tuesday, April 17: continued
- Thursday, April 19: The equity premium puzzle  
 LS Sections 13.12-13.14  
 Mehra, Rajnish, and Edward Prescott (1985), "The Equity Premium: A Puzzle", JME 15, 2 (March), 145-162.
- Tuesday, April 24: Other empirical failures of the model and proposed solutions  
 Problem: consumption too sensitive to current income  
 Proposed solutions: borrowing constraints  
 buffer stock saving  
 Deaton, 1991, "Saving and Liquidity Constraints", Econometrica, 59, 1221-48.  
 Caballero, 1990, "Consumption Puzzles and Precautionary Savings", Journal of Monetary Economics, 113-136.  
 Carroll, 1997, "Buffer Stock Saving and the Life Cycle/Permanent Income Hypothesis", Quarterly Journal of Economics.  
 Gourinchas and Parker, 2002, "Consumption over the Life-cycle", Econometrica, 47-89.
- Thursday, April 26: Problem: consumption "too smooth" (i.e., extremely low EIS)  
 Proposed solutions: habit persistence  
 Epstein-Zin preferences  
 Constantinides, George (1990), "Habit Formation: A Resolution of the Equity Premium Puzzle", JPE 98, 3 (June), 519-543.  
 Abel, Andrew (1990), "Asset Prices under Habit Formation and Catching up with the Joneses", AER Papers and Proceedings, 80 (May 1990), 38-42.  
 Dynan, Karen E. (2000), "Habit Formation in Consumer Preferences: Evidence from Panel Data", AER 90 (June 2000), 391-406.  
 Epstein and Zin, 1991, "Substitution, Risk Aversion and the Temporal Behavior of Consumption and Asset Returns: An Empirical Analysis", Journal of Political Economy, 99, 263-86.
- Tuesday, May 1: Beyond the standard model: Non-separable utility and adjustment costs (housing models)  
 Grossman, Sanford J., and Laroque, Guy (1990). "Asset Pricing and Optimal Portfolio Choice in the Presence of Illiquid Durable Consumption Goods", Econometrica, 58, (1) pp 25-51.  
 Caballero, Ricardo J. (1993). "Durable Goods: An Explanation for Their Slow Adjustment", Journal of Political Economy, 101 (2) pp. 107-17.  
 Flavin, Marjorie, and Shinobu Nakagawa (2008) "A Model of Housing in the Presence of Adjustment Costs: A Structural Interpretation of Habit Persistence", American Economic Review
- Thursday, May 3: **Final exam**