

Economics 210Ba: Macroeconomics
Winter 2013

Professor Marjorie Flavin

lectures: Tuesday and Thursday, 11:00-12:20, room 300

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office hours: Wednesdays 1:00 – 3:00

TA: Mike Levere

office hours: Tuesdays 2:00 – 3:00

TA session: Thursdays 2:00 – 3:20

Econ 210B consists of two independent components, with this course, 210Ba taking the first five weeks of the quarter and the second component, Econ 210Bb, taught by Irina Telyukova, taking the last 5 weeks of the quarter. The in-class exam on Thursday, February 7 will be 80 minutes in length and will serve as the final for the 210Ba component. Your course grade for 210B as a whole will be the average of your grades on the two components.

Problem sets will be assigned approximately weekly, and will be due in class on Tuesdays. Mike will grade the problem sets and go over the solutions in his weekly TA session. 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

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

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

Note: When the appropriate sections of Ljungqvist and Sargent are different in the second and third editions, the sections for the second edition are listed first. The sections for the third edition are listed second and in brackets and italics.

Schedule of lectures and related reading

Tuesday, Jan 8: Equilibrium consumption allocation under complete markets;
Arrow-Debreu market structure; trades occur at time zero
LS Sections 8.1-8.7

Thursday, Jan 10: continued

Tuesday, Jan 15: Equilibrium consumption allocation under complete markets;
sequential trading with one-period Arrow securities
LS Sections 8.8-8.10, 8.13, 8.18 [8.8-8.12]

Thursday, Jan 17: continued

Tuesday, Jan 22: Euler equations
with certainty equivalence (permanent income model)
without certainty equivalence (general model)
LS Sections 13.1-13.3 [13.1-13.2]
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, Jan 24: Consumption-beta model (C-CAPM)

LS Sections 13.4-13.9 [13.3-13.8]

Lucas (1978), "Asset Prices in an Exchange Economy," *Econometrica*, 46, 6 (Dec), 1426-1445.

Blanchard and Fischer, pp 279-291 and 506-512

Tuesday, Jan 29: The equity premium puzzle

LS Sections 13.12-13.14 [14.1-14.3]

Mehra, Rajnish, and Edward Prescott (1985), "The Equity Premium: A Puzzle", JME 15, 2 (March), 145-162.

Thursday, Jan 31: 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.

Tuesday, Feb 5: Problem: consumption “too smooth” (i.e., extremely low EIS)

Proposed solutions: habit persistence
Epstein-Zin preferences
adjustment costs on housing

[LS 14.7]

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.

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, Feb 7: **Final exam**