

Volatility Accounting: A Production Perspective on Increased Economic Stability

Kevin Stiroh

This paper examines the declining volatility of U.S. output growth from a production perspective. At the aggregate level, increased output stability reflects decreased volatility in both labor productivity growth and hours growth, as well as a significant decline in the covariance. The decline in output volatility can also be traced to less volatile labor input and total factor productivity (TFP) growth and the smaller covariance between them. At the industry-level, the decline in volatility appears widespread with about 80% of component industries showing smaller contributions to aggregate output volatility after 1984, although most of the aggregate decline reflects smaller covariances between industries. There is also strong evidence of a decline in the correlation between hours and labor productivity growth across industries. The paper concludes with a discussion of potential explanations.

What explains the Great Moderation in the US? A Structural Analysis

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This paper investigates what has caused output and inflation volatility to fall in the US using a small scale structural model using Bayesian techniques and rolling samples. There are instabilities in the posterior of the parameters describing the private sector, the policy rule and the variance of the shocks. Results are robust to the specification of the policy rule. Changes in the parameters describing the private sector are the largest, but those of the policy rule and the covariance matrix of the shocks explain the changes most.

The Time-Series Properties of Aggregate Consumption: Implications for the Costs of Fluctuations

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The properties of the stochastic process followed by aggregate consumption affect the estimates of the costs of fluctuations. This paper pursues two approaches to modelling consumption dynamics and measuring how much society dislikes fluctuations, one statistical and one economic. The statistical approach estimates the properties of consumption and calculates the costs of having consumption fluctuating around its mean growth. The paper finds that persistence is a crucial determinant of the costs and that the high persistence in the data severely distorts conventional measures. It shows how to compute valid estimates and confidence intervals. The economic approach uses a calibrated model of optimal consumption and measures the costs of eliminating income shocks. This uncovers a further cost of uncertainty, through its impact on precautionary savings and investment. The two approaches lead to costs of fluctuations that are higher than the common wisdom, between 0.5% and 5% of per capita consumption.

The Effect of Plant Downsizing on Disability Pension Utilization

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We investigate the impact of plant downsizing on disability pension utilization in Norway. Plant downsizing substantially increases the disability entry rate of workers in affected plants. Workers originally employed in plants that downsized by more than 60 percent between 1995 and 2000 were 24 percent more likely to utilize disability pensions in 2001 than comparable workers in non-downsizing plants. We also estimate significant effects of downsizing on future earnings and mortality, which suggest the increase in disability participation could be driven by an adverse effect of downsizing on the economic opportunities or the health of affected workers.

Exchange Rates and Fundamentals: Footloose or Evolving Relationship?

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Using novel real-time data on a broad set of economic fundamentals for five major US dollar exchange rates over the recent float, we employ a predictive procedure that allows the relationship between exchange rates and fundamentals to evolve over time in a very general fashion. Our key findings are that: (i) the well-documented weak out-of-sample predictive ability of exchange rate models may be caused by poor performance of model-selection criteria, rather than lack of information content in the fundamentals; (ii) the difficulty of selecting the best predictive model is largely due to frequent shifts in the set of fundamentals driving exchange rates, which can be interpreted as reflecting swings in market expectations over time. However, the strength of the link between exchange rates and fundamentals is different across currencies.

Is Transparency about Central Bank Plans Desirable?

Anne Sibert, Birkbeck College

A central bank with private information about its preferences has an incentive to reduce its planned inflation to increase the public's perception of its inflation aversion and lower expected future inflation. A regime is said to be transparent if planned inflation is observable and reveals the central bank's preferences and to be non-transparent if planned inflation is unobservable and can be only imperfectly inferred from actual inflation. A central bank in the non-transparent regime is said to become more transparent when actual inflation becomes a better signal of planned inflation. I find several results about transparent and non-transparent regimes: some are novel and some contrast with the results of earlier papers. In particular, I demonstrate that in a non-transparent regime, increased transparency need not improve the public's ability to infer a central bank's private information. I show that society and central banks are better off with more transparency. My numerical results suggest that society and central banks prefer the transparent to the non-transparent regimes.

New Evidence on the Interest Rate Effects of Budget Deficits and Debt

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Estimating the effects of government debt and deficits on Treasury yields is complicated by the need to isolate the effects of fiscal policy from other influences. To control for the effects of the business cycle, and associated monetary policy actions, on debt, deficits, and interest rates, this paper studies the relationship between long-horizon forward rates and future federal government deficits and debt as projected by the Congressional Budget Office. For the entire 30-year sample for which these projections are available, the estimated effects of government deficits and debt on interest rates are statistically significant and economically relevant: about 25 basis points per percentage point increase in the projected deficit/GDP ratio, and 3 to 4 basis points for the debt/GDP ratio. Under plausible assumptions the parameter estimates are shown to be consistent with predictions from the neoclassical growth model.

Deception and Misreporting in a Social Program

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We investigate empirically the extent of misreporting in a poverty-alleviation program in which self-reported information, followed by a household visit, is used to determine eligibility. In the model we propose and estimate, underreporting may be due to a deception motive, and overreporting to an embarrassment motive. We find that underreporting of goods and desirable home characteristics is widespread, and that overreporting is common with respect to goods linked to social status. Larger program benefits encourage underreporting and discourage overreporting. We also estimate the costs of lying and embarrassment for different goods, and show that the embarrassment cost for lacking a good is proportional to the percentage of households who own the good.