Rethinking Macroeconomics: What Went Wrong and How to Fix It
Joseph E. Stiglitz, Columbia University

Standard macroeconomic models have failed, by all the most important tests of scientific theory: They did not predict that the financial crisis would happen, and even when it did, they miscalculated its effects and provided little guidance on how to respond. Policies based on the standard models contributed to the crisis—which the models said couldn’t happen. This paper first describes the failures of the standard models in broad terms. While providing micro-foundations for macroeconomics is essential, they have to be the right microfoundations, which includes incorporating problems arising from information asymmetries (including agency) and imperfect risk markets. This crisis illustrates that the most important shocks confronting an economy are endogenous, and the importance of careful modeling of credit and the financial system. The paper develops the economics of deep downturns, analyzing the sources of disturbances, why disturbances get so amplified, and why recoveries are so slow. The paper argues that there have been systemic changes to the structure of the economy that made the economy more vulnerable to crisis, contrary to what the standard models argued. Finally, the paper contrasts the policy implications of our framework with those of the standard models.

Workers, Warriors, and Criminals: Social Conflict in General Equilibrium
Ernesto Dal Bó, UC Berkeley and Pedro Dal Bó, Brown University

We incorporate appropriation activities ("social conflict") into canonical models of trade and study how economic shocks and policies affect the intensity of conflict. We show that not all shocks that could make society richer reduce conflict: positive shocks to labor intensive industries diminish conflict, while positive shocks to capital intensive industries increase it. The key requirement is that conflict activities be more labor intensive than the economy as this determines how shocks affect the returns and costs of conflict. Our theory is consistent with several observed patterns of conflict and implies that empirical work should take into account the relative factor intensities of the productive and conflict sectors in each country. Incorporating appropriation into a canonic general equilibrium model affects what policies may be deemed desirable: in order to reduce conflict and generate Pareto-improvements policy must be distortionary, while reforms that appear efficiency-enhancing under the unrealistic assumption of perfect property rights may backfire. This offers one explanation for why reforms based on traditional models without appropriation may be delayed and become unpopular when implemented, and why societies may sympathize with seemingly inefficient redistribution. (JEL: D74, D78, F13, H23, K42, O1)

Crime and Police Resources: The Street Crime Initiative
Stephen Machin, University College London and London School of Economics and Olivier Marie, Maastricht University, Royal Holloway, University of London and LSE

In this paper we look at the connection between police resources and crime by focusing on a large-scale policy intervention - the Street Crime Initiative - that was introduced in England and Wales in 2002. This allocated additional resources to some police force areas to specifically target street crime, whereas other forces did not receive any additional funding. Estimates derived from several empirical strategies show that robberies fell significantly in SCI police forces relative to non-SCI forces after the initiative was introduced. Moreover, the policy seems to have been a cost effective one, even after extensively testing for possible displacement or diffusion effects onto other crimes and into adjacent areas. Overall, we reach the conclusion that increased police resources can be used to generate falls in crime, at least in the context of the SCI programme we study. (JEL: H00, H5, K42)
**Countervailing Power and Dynamic Efficiency**

*Roman Inderst, Goethe University Frankfurt and Imperial College London and Christian Wey, DIW Berlin and TU Berlin*

This paper studies the impact of buyer power on dynamic efficiency. We consider a bargaining model in which buyer power arises endogenously from size and may impact on a supplier's incentives to invest in lower marginal cost. We challenge the view frequently expressed in policy circles that the exercise of buyer power stifles suppliers' incentives. Instead, we find that the presence of larger buyers keeps a supplier "more on his toes" and induces him to improve the competitiveness of his offering, in terms of both price and quality, relative to buyers' alternative options. (JEL: L25, L41)

**Buyer Power and Intrabrand Coordination**

*Jeanine Miklós-Thal, University of Rochester, Patrick Rey, Toulouse School of Economics, and Thibaud Vergé, CREST*

We analyse the competitive effects of various contractual provisions in a situation where rival retailers make offers to a common manufacturer. In contrast to Marx and Shaffer (2007), who find that a strong retailer can use slotting allowances (that is, upfront payments from manufacturers) to exclude its weaker rival, we show that foreclosure is no longer inevitable once retailers’ offers can be contingent on the relationship being exclusive or not. There then exist equilibria that sustain the industry monopoly outcome; moreover, as long as retailers can use non-linear tariffs, such equilibria exist irrespectively of whether slotting allowances are allowed or banned. Non-contingent contracts, on the other hand, necessarily lead to exclusion, with or without slotting allowances. A ban on slotting allowance may therefore prove ineffective, while a ban on exclusive dealing options in supply contracts leads to foreclosure. (JEL: L14, L42)

**Long-Run Effects Of Public Sector Sponsored Training In West Germany**

*Michael Lechner, University of St. Gallen, Ruth Miquel, University of St. Gallen, and Conny Wunsch, University of St. Gallen*

We estimate the short-, medium- and long-run effects of different types of government-sponsored training in West Germany using particularly rich data which allows to control for selectivity by matching methods and to measure interesting outcome variable over eight years after programme start. We use distance weighted radius matching with a weighted-regression-based bias removal procedure to increase precision and robustness of standard matching estimators. We find negative employment effects in the short-run for all programme types whose magnitude and length of occurrence is directly related to programme duration. In the longer run training seem to increase employment rates by about 10 to 20%-points. For both the shortest and the longest, most intensive programme type these positive effects seem to be sustainable over the eight-year observation period. (JEL: J68)

**Monitoring in Teams: Using Laboratory Experiments to Study a Theory of the Firm**

*Stefan Grosse, University of Erfurt, Louis Putterman, Brown University, and Bettina Rockenbach, University of Erfurt*

Alchian and Demsetz’s (1972) influential explanation of the classical business firm argues that there is need for a concentrated residual claim in the hands of a central agent, to motivate the monitoring of workers. We model monitoring as a way to transform team production from a collective action dilemma with strong free riding incentives to a productivity-enhancing opportunity with strong private marginal incentives to contribute effort. In an experiment, we have subjects experience team production without monitoring, team production with a central monitor, and team production with peer monitoring, then vote on whether to employ the central monitor, who gets to keep a fixed share of the team output, or to rely on peer monitoring, which entails a coordination or free riding problem. Our subjects usually prefer peer monitoring but they switch to the specialist when unable to successfully self monitor. We provide evidence for situations in which team members resist the appointing of a central monitor and succeed in overcoming coordination and free riding problems as well as for a situation in which an Alchian-Demsetz-like firm “grows” in the laboratory. (JEL: C92, D20, D70, H41, J54, P12, P13)