ABSTRACTS OF WORKING PAPERS IN ECONOMICS

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Abbott, Michael G.
PD December 1987. TI Immigrant Earnings Differentials and Cohort Effects in Canada. AU Abbott, Michael G.; Beach, Charles M. AA Queen's University.
AB This paper examines what has happened to immigrant earnings in Canada and tests two alternative hypotheses of Chiswick and Borjas. The paper uses a 1973 survey containing detailed information on immigrant status, family background, and a direct measure of work experience. It is found that earnings differentials of immigrant men have been widening since later 1960's. This is due to a steepening of earnings profiles for native workers (supporting Chiswick), a flattening of the years-since-migration earnings profile for immigrants (supporting Borjas), and a further flattening of the experience-earnings profile of immigrants.

Abraham, Katherine G.
AB One of the most prominent features of United States unionism is the key role played by seniority. However, in cross-sectional data, the positive association between seniority and earnings is typically much stronger for nonunion workers than for union workers. This finding has puzzled previous researchers, since it seems inconsistent with the generalization that seniority is more important in the union sector than in the nonunion sector. We show that standard estimates of the return to seniority are likely to be biased upward and argue that the bias is likely to be larger in the nonunion sector than in the union sector. Corrected estimates imply that the return to seniority is, in fact, larger in the union sector than in the nonunion sector.

Adelman, Irma
AB This paper employs the Social Accounting Matrix (SAM) to analyze the economic structure of a migrant-sending rural economy. A village SAM is constructed using 1982 household data from a major migrant-sending village in Central Mexico. The village matrix multiplier and its decompositions are derived from the SAM and are utilized in policy experiments on the production, value added, income, and investment flows of the village. The results highlight the central role of both internal and international migration in the village economy, as well as importance of targeting directly anti-poverty policies toward the landless.

Adioetomo, Sri M.
PD October 1987. TI Change in the Status of Women Across Generations in Asia. AU King, Elizabeth; Peterson, Jane; Adioetomo, Sri M.; Domingo, Lita; Syed, Sabiha H.
Aigner, Dennis J.
AB In none of the existing studies that attempt to pool the results of the five best residential electricity TOU-pricing experiments is the problem of selection bias addressed. Three of the five experiments used samples of volunteers and it is well-known that this can bias results if the ultimate inference to be made applies to the population of non-volunteers (i.e., the situation of mandatory TOU-pricing). In this paper we adapt some well-used
Aizenman, Joshua
PD August 1987. TI Market Power and Exchange Rate Adjustment in the Presence of Quotas. AA University of Chicago. SR National Bureau of Economic Research Working Paper: 2870; National Bureau of Economic Research, 1050 Massachusetts Avenue, Cambridge, MA 02138. PR $2.00. JE 431, 023, 422, 421. KW Exchange Rates. Quotas. Pass-through. Commercial Policy. Tariffs. AB This paper investigates the dependency of the adjustment of prices, exchange rates, and production on the nature of the trade regime. We contrast the adjustment between a quota and a tariff regime for a semi-small economy characterised by monopolistic competitive market structure and short-run nominal contracts under a floating exchange rate regime. Among other issues we focus on the factors determining the behavior of the quota rent and the 'pass-through' of exchange rate adjustment to the domestic prices of importable goods. We demonstrate that the 'pass-through ratio' (measuring the elasticity of the domestic price of importable goods with respect to the exchange rate) is determined by both the commercial policy and by the market power of the various producers. It tends to be higher in a tariff regime because the endogenous adjustment of the quota rent mitigates the 'pass-through'. We also show that the adjustment of the exchange rate tends to be larger in the quota regime than in the tariff regime. In the tariff regime we observe a larger switch of domestic demand relative to the quota regime, and a corresponding smaller exchange rate adjustment. In the quota regime we observe adjustment of the quota rent such as to keep the net domestic demand for foreign goods intact. As a result, the relative price of the foreign good facing the foreign consumer adjusts more in the quota regime than in the tariff regime. At the same time the relative price facing domestic consumers in the quota regime adjusts by less than in the tariff regime.

Alesina, Alberto
PD August 1987. TI An Overlapping Generations Model of Electoral Competition. AU Alesina, Alberto; Spear, Stephen. AA Carnegie-Mellon University. SR National Bureau of Economic Research Working Paper: 2554; National Bureau of Economic Research, 1050 Massachusetts Avenue, Cambridge, MA 02138. PR $2.00. JE 052. KW Politics. Political Parties. Elections. Overlapping Generations. Policymakers. Candidates. AB This paper presents a dynamic model of political competition between two "parties" with different policy preferences. A "party" is explicitly modelled as a sequence of overlapping generations of candidates, all of whom face finite decision horizons. In general, there is a conflict between the interests of the individual policymakers and those of the "party", which includes subsequent generations of candidates. We characterize this conflict and suggest a scheme of "intergenerational transfers" within the party which can resolve or mitigate this conflict. The paper shows how the overlapping generations model can be usefully applied to the political arena.

Alexander, Lewis S.
PD November 1987. TI Debt Conversions: Economic Issues for Heavily Indebted Developing Countries. AA Division of International Finance, Board of Governors of the Federal Reserve System. SR Board of Governors of the Federal Reserve System International Finance Discussion Paper: 315; Division of International Finance Board of Governors of the Federal Reserve System, Washington, D.C. 20551. PG 39. PR No Charge. JE 112, 433, 441, 442. KW Debt-for-Equity Swaps. Debt and Development. AB This paper is a general discussion of debt conversions in heavily indebted developing countries. The paper first describes the three different types of transactions that are commonly called debt conversions. Next the paper discusses programs that have been established in Chile, Brazil, Mexico, Argentina, and the Philippines to facilitate these transactions. Then the different ways in which commercial banks can participate in these transactions and the volume of these transactions to date are discussed. The paper concludes with a discussion of a broad range of economic issues raised by these transactions, including: the effect of debt conversions on the structure of debtor countries' external liabilities, the incentives debt conversion programs provide for net new capital inflows, the macroeconomic effects of these transactions, and the new role for debt swaps programs in the so-called "menu-of-options" approach to restructuring developing countries' bank debts.

Allard, Marie
PD 1987. TI Roy-Consistent Expectations. AU Allard, Marie; Brionard, Camile; Richelle, Yves. AA Allard, Richelle: CORE. Bronnard: University of Montreal. SR Université Catholique de Louvain CORE Discussion Paper: 8734; Université Catholique de Louvain Voie du Roman Pays, 34, B-1348 Louvain-la-Nuée BELGIUM. PG 23. PR No Charge. JE 022. KW Expectations. Demand. Polemarchakis Theorem. AB In this paper we define a new class of expectations which, under proper specification, implies either the exogenous expectations case or the static expectations one or the rational expectations hypothesis. This class allows thus to bridge the gap between arbitrary expectation functions (like those used in the temporary equilibrium framework - see Grandmont (1983)) and rational expectations. On the other hand, with this class of expectations it is shown that the short-run demands
display some of the neo-classical properties, and this is a partial answer to the Polemarchakis (1983) theorem about
the arbitrariness of the short-run demands.

Allen, Linda
AB Banks' purchase behavior in the Federal funds (FF) market has been the subject of considerable anecdotal evidence (see, for example Lucas, Jones and Thurston, 1977. Maerowitz 1981, and Stigum 1982, who describe the tendency of large banks, located in major banking centers, to be net purchasers of FF while smaller banks, located away from major money centers, tend to act as net sellers). Yet, despite the central importance of the FF market to the determination of interest rates and the transmission of monetary policy, no study has rigorously documented either the existence of such a dichotomy in bank net purchase behavior or the size segmentation point (if any) that differentiates bank net sellers from net purchasers. The objective of this paper is to use individual bank data on FF purchases and sales to analyze this question and to examine whether differential behavior can be linked to well defined characteristics such as size and location. In so doing we also contrast bank net purchase behavior in the uncollateralized FF market with bank activity in the collateralized market for repurchase agreements (repos).

Allen, Steven G.
TI Pension Wealth, Age-Wealth Profiles, and the Distribution of Net Worth. AU McDermed, Ann; Clark, Robert L.; Allen, Steven G.

Alon, N.
AB Suppose we have k points in general position in the plane such that the ratio between the maximum distance of any pair of points to the minimum distance of any pair of points is at most alpha times the square root of k, for some positive constant alpha = beta(alpha). On the other hand we show that for every fixed epsilon > 0, if k > k(epsilon), then there is a set of k points in the plane for which the above ratio is at most 4 times the (square root of k), which does not contain a convex polygon of more than k to the 1/3 + epsilon vertices.

Anderson, Simon P.
AB We assess here the effects of government regulation of spatial pricing policies. Two regulatory policies are considered. Under the first, firms are constrained to mill pricing. Under the second they are obliged to price uniformly over space. These policies are compared, in a duopoly model, to the unregulated market equilibrium characterised by spatial price discrimination. In contrast to the monopoly case, it is found that consumer surplus is highest under uniform delivered pricing and lowest under mill pricing, whereas profit and social surplus follows the opposite ranking. Government regulation to encourage mill pricing may therefore benefit firms to the detriment of consumers.

Arnott, Richard
AB This paper is concerned with the modelling of congestable facilities subject to peak-load demand. It argues that a properly-specified model should explicitly treat the congestion technology and consumers' time-of-use decision. The standard model of peak-period congestion can be interpreted as the reduced form of such a model if the peak period is treated as a single interval, but not if it is divided into sub-intervals. To illustrate these points, the paper extends Vickrey's model of bottleneck congestion, treating elastic demand and solving for optimal capacity under several pricing regimes.

Ashley, Richard
PD July 1987. TI On the Accuracy (or Otherwise) of Recent Macroeconomic Forecasts. AA Virginia Polytechnic Institute and State University. SR Virginia Polytechnic Institute and State University Working Paper in Economics: E87-10-01; Department of Economics, Virginia Polytechnic Institute and State University,
AB The accuracy of recent forecasts of key macroeconomic variables by a variety of forecasters is analysed. It is shown that most of these forecasts are so inaccurate that simple extrapolation of historical trends is superior for forecasts more than a couple of quarters ahead. The implications of these results for the appropriate modelling of macroeconomic expectations formation are discussed.

AB Shrinkage estimation is analysed using stochastic dominance theory over a wide class of loss functions. (Neither symmetry nor boundedness is imposed.) A recommended shrinkage factor is calculated for gaussian, unbiased estimators based on this analysis. This factor, which depends only on the observed t statistic and on a parameter specifying the degree of asymmetry of the loss functions in the class, maximizes the probability that the resulting shrinkage estimator both dominates the original unbiased estimator and is itself undominated over the loss function class. Also, the unbiased estimator is found to be dominated by shrunk (biased) estimators over a wide class of loss functions. This implies that the unbiased linear projections used to model expectations formation in neoclassical macroeconomic models are stochastically dominated by biased expectations.

AB A statistical test based on the estimated bispectrum is presented which can distinguish between the linear stochastic dynamics widely used in macroeconomic models and alternative nonlinear dynamic mechanisms, including both nonlinear stochastic models and nonlinear deterministic (chaotic) models. The test is applied to an aggregate stock market index and to an aggregate industrial production index. In both cases the test easily rejects the null hypothesis of a linear stochastic generating mechanism. This result suggests that nonlinear dynamics (deterministic or stochastic) should be an important feature of any empirically plausible macroeconomic model.

Attanasio, Orazio P.
AB In this paper we investigate the empirical relevance of two theoretical issues concerning life cycle consumer optimizing behaviour: the possibility of disentangling the concepts of risk aversion and intertemporal substitution, and the plausibility of the assumptions needed for the dynamic view of intertemporal maximisation to be correct. We use Selden’s Ordinal Certainty Equivalence approach to separately identify the coefficient of relative risk aversion and the elasticity of intertemporal substitution and jointly estimate a consumption growth and two asset return Euler equations. We alternatively use aggregate data and average cohort data to assess the importance of aggregation bias. Finally, we provide an alternative interpretation of our results in the light of Kreps and Porteus (1978) analysis of behaviour under uncertainty.

Bagnoli, Mark
AB We have reported on some experiments run using, as a basis, a game studied by Bagnoli and Lipman. Their analysis suggested that if people used strategies that constituted a proper equilibrium, then the equilibria of the game generated the efficient outcome. Our experiments clearly indicate that in the final 5 periods of the game, the participants always provided the public good (the efficient choice as we had chosen parameters that made the participants' valuations sum to more than the cost of the public good). Thus, it appears sensible to focus on the proper equilibria of the game under analysis. Second, we have shown that this game is likely to eliminate virtually all of the free rider problems one normally fears may cause the private provision of a public good to be inefficient. Third, we have provided evidence concerning the effects of studying games of private provision of public goods that do not have the unsavory feature of a dominant strategy.

Ball, Laurence
This paper studies the welfare properties of the equilibrium timing of price changes. Staggered price-setting has the advantage that it permits rapid adjustment to firm-specific shocks but the disadvantage that it causes price level inertia and therefore increases aggregate fluctuations. Because each firm ignores its contribution to inertia, staggering can be a stable equilibrium even if it is highly inefficient. In addition, there can be multiple equilibria in the timing of price changes; indeed, whenever there is an inefficient staggered equilibrium, there is also an efficient equilibrium with synchronised price-setting.

Banks, Jeffrey S.

This paper demonstrates the use of applied organisational design to investigate possible mechanisms to allocate the resources of Space Station. First, a specific laboratory experimental environment (testbed) and baseline policy are developed using the salient technical features of the Space Station and past Space Shuttle experiences. The use of priority contracts to assist in contingent rescheduling of resources due to supply curtailments is established. Next, generalized versions of an English auction and Vickrey-Groves type sealed bid auction are designed and developed to allocate scheduled resource use and priority. Finally, these mechanisms are tested and evaluated in the testbed. The data demonstrates that the expected efficiency increases significantly using the auction mechanisms rather than allocations from first-come-first-served processes. However, the auction mechanisms do not produce outcomes near the 100 per cent level of efficiency. Several results are dedicated to the revenue generating properties of the mechanisms and individual bidding behavior.

Barahona, Francisco

For planar graphs Seymour proved that there is a multicommodity flow if and only if there is no negative cut. Matsumoto et al. have shown how to find the flow by solving \(O(\eta)\) matching problems in a graph with \(\eta\) nodes. Our aim is to point out that the flow can be found by solving a single Chinese Postman problem in the dual graph. The dual vector is the flow. Thus the problem can be solved in \(O(\eta \sup 3/2 \log \eta)\) time. The same ideas apply to the max cut problem in planar graphs.

Barsky, Robert
PD June 1987. TI The Seasonal Cycle and the Business Cycle. AU Barsky, Robert B.; Miron, Jeffrey A. AA University of Michigan and NBER. SR University of Michigan Center for Research on Economic and Social Theory Working Paper: 87-34; Department of Economics, University of Michigan, Ann Arbor, MI 48109. PG 47. PR No Charge. JE 131, 023, 212. KW Seasonal Fluctuations.

Almost all recent research on macroeconomic fluctuations has worked with seasonally adjusted or annual data. The usual attitude toward seasonal fluctuations is typified by Sims (1974), who refers to the seasonal components of economic time series as "errors in variables" and analyses methods for treating series "contaminated by seasonal noise." Perhaps underlying this view is the notion that seasonal fluctuations are entirely natural or even desirable while business cycle fluctuations are disturbing aberrations. This paper takes a different approach by treating seasonal fluctuations as worthy of study in their own right. Instead of taking it for granted that seasonal fluctuations follow a fundamentally different model than conventional business cycle fluctuations. Many economists would argue that seasonal fluctuations are entirely natural or even desirable while business cycle fluctuations are disturbing aberrations. This paper takes a different approach by treating seasonal fluctuations as worthy of study in their own right. Instead of taking it for granted that seasonal fluctuations follow a different model from business cycle fluctuations, we consider the extent to which the two types of fluctuations display similarities. Our paper represents a return to an older tradition of NBER analysis of fluctuations, exemplified by Simon Kuznets (1933), in which fluctuations at both seasonal and business cycle frequencies were regarded as important topics of investigation.

PD July 1987. TI The Worldwide Change in the Behavior of Interest Rates and Prices in 1914. AU Barsky, Robert; Mankiw, N. Gregory; Miron, Jeffrey; Weil, David. AA Barsky, Miron: University of
Michigan.
AB This paper evaluates the role of the destruction of the gold standard and the founding of the Federal Reserve, both of which occurred in 1914, in contributing to observed changes in the behavior of interest rates and prices after 1914. The paper presents a model of policy coordination in which the introduction of the Fed stabilizes interest rates, even if the gold standard remains intact, and it offers empirical evidence that the dismantling of the gold standard did not play a crucial role in precipitating the changes in interest rate behavior.
AB This paper evaluates the role of the destruction of the gold standard and the founding of the Federal Reserve, both of which occurred in 1914, in contributing to observed changes in the behavior of interest rates and prices after 1914. The paper presents a model of policy coordination in which the introduction of the Fed stabilizes interest rates, even if the gold standard remains intact, and it offers empirical evidence that the dismantling of the gold standard did not play a crucial role in precipitating the changes in interest rate behavior.

Bartusch, M.
AB Project networks with time windows are generalizations of the well-known CPM and MPM networks that allow for the introduction of arbitrary minimal and maximal time lags between the starting and completion times of any pair of activities. We consider the problem to schedule such networks subject to arbitrary (even-time dependent) resource constraints in order to minimise an arbitrary regular performance measure (i.e. a non-decreasing function of the vector of completion times). This problem arises in many standard industrial construction or production processes. The treatment is done by a structural approach that involves a generalization of both the disjunctive graph method in job shop scheduling and the order theoretic methods for precedence constrained scheduling. Besides theoretical insights into the problem structure, this approach also leads to rather powerful branch-and-bound algorithms. Computational experience with this algorithm is reported.

Beach, Charles M.
TI Immigrant Earnings Differentials and Cohort Effects in Canada. AU Abbott, Michael G.; Beach, Charles M.

Beja, Avraham
AB This (short) study reports an application of the Shapley value axioms to a new context of "two-stage games". In these games, the formation of a coalition in the first stage entitles its members to play a prespecified cooperative game in the second stage. The original Shapley axioms have natural equivalents in the new framework, and we show the existence of (non-unique) "values" and "semivalues" for two-stage games, analogous to those defined by the corresponding axioms for simple (one-stage) games. However, we also prove that all semivalues (hence, perforce, all values) must give patently unacceptable solutions for some "two-stage majority games" (where the members of a majority coalition play a conventional majority game). Our analysis is closely related to an example of Roth (1980), who pointed out difficulties with Shapley's "lambda-transfer value" for non-transferable utility (NTU) games. Comparing our findings with Roth's, we argue that our results are more conclusive. Furthermore, the value axioms for two-stage games are much closer to Shapley's original axioms than are the axioms for the "NTU value". Our analysis therefore also sheds new light on the original Shapley value.

Bernhardt, Dan
AB Sticky nominal prices represent a cornerstone of many macroeconomic models. The effects of costly price adjustment on strategic firm interaction and the resulting price series implications are less established. This paper develops a spatial economy in which these interactions can
be analysed. In the two period environment, each firm, facing menu costs, must choose (whether to adjust) the price of its spatially identified good in the Bayesian Nash competition. As heterogeneity increases or competition decreases, prices are less frequently adjusted. These findings accord with empirical work which find that markets with more heterogeneous goods which are less competitive (e.g. labor) have stickier prices than others (e.g. wheat). Firms tend to adjust prices in concert and to be more responsive toward shocks which lead to price increases than decreases, as has been documented empirically. The magnitude of menu costs affect the ability of firms to collude, so expected profits may increase with menu costs. Thus, the model provides a twist to the classic kinked demand theory.

Bhattacharya, Sudipto

AB The performance of tournament incentive schemes is compared with that of schemes based on termination threats, in an environment with two-sided moral hazard for both principal and agent, and "moving support" monitoring. The disadvantages of the former scheme that arise from having to eliminate "collusive" multiple equilibria among agents are contrasted with the "involuntary unemployment" deadweight-loss of termination-based schemes. Circumstances for dominance of one scheme over the other are identified.


AB The design of optimal multi-agent incentive contracts has been the focus of much recent research on moral hazard, i.e., contractual inducement of unobservable actions taken by agents, given contracts designed by principals. Given the rapid pace of developments in this area, particularly on results associated with a scenario of a large set of ex ante homogeneous agents, the original empirical context which perhaps motivated the pioneering work of Lazear and Rosen has tended to become somewhat overlooked. Specifically, leaving aside state lotteries and football pools, tournament contracts are largely observed in the economic context of hierarchical organizations. In particular, the empirically observed contests typically have in each a restricted set of participants that is far smaller than the size of the organization which, at the top, is thought of as the principal. It is also the case that in most observed contests, agents who are compared with each other in order to determine wages and promotions work in the same or highly contiguous levels of the hierarchy in question. Most analytical models of hierarchies (e.g., Rosen '1982) would thus suggest that the inherent ability levels of participants, is (approximately) homogeneous within contests and heterogeneous across them. We seek to explain such "within cohorts" tournaments endogenously.


AB We examine a two-stage model of research and development (R&D) contests. A social planner designs the R&D contest in an attempt to maximize expected social surplus. At the second stage, researchers choose R&D effort levels independently in an attempt to successfully achieve an innovation of value V. In the first stage, researchers are afforded the opportunity to share with one another the productive knowledge with which they are endowed. All rewards for disclosing production knowledge and for succeeding at the second stage can only be paid when the innovation is realized successfully. Also, the sum of all payments cannot exceed V. Thus, internal financing is required. We derive necessary and sufficient conditions for the social planner to be able to motivate both full sharing of knowledge and the socially desired levels of R&D effort. We also examine the optimal incentive structure when this ideal outcome cannot be implemented. We find that full sharing of information will always be motivated at the first stage, but that inefficiently high or low R&D effort levels will be induced to better foster information sharing.


AB We consider a two-stage model of research and development (R&D). In the second stage, researchers simultaneously choose unobservable effort levels to develop an innovation of known value. In the first stage, researchers who are randomly endowed with different levels of research knowledge can transfer some or all of their realized knowledge to competitors. We examine the ability of two incentive mechanisms to ensure both efficient sharing of knowledge and subsequent expenditure of the efficient levels of R&D effort, i.e., to attain the First-Best outcome. The Full-Surplus mechanism, in which less knowledgeable agents pay their expected profits from continued second-stage participation to the most knowledgeable agent, is shown to ensure the First-Best outcome. The Tie-Surplus mechanism, in which such inter-agent transfers are not feasible, can also implement...
the First-Best outcome in some circumstances, but will not always do so. Asymptotically, as the optimal number of researchers becomes large, the performance of these two mechanisms converge.

**Bigelow, John**


AB In this paper, we consider the provision of product warranties when the exit of existing firms is possible. When firms' precommitment to market participation is credible, warranties can provide insurance against product failure to risk averse consumers. In the absence of such precommitment, firms have the option of leaving the market if continued participation is not profitable, thereby avoiding outstanding warranty obligations. Thus, the value of a warranty today depends on the likelihood that the firm will remain in business in the future which depends, in turn, on future profits. Since future profits depend on future sales, warranty contracts generate an intertemporal linkage between consumers of different generations. For economies in which credible commitment to participation is not feasible, this linkage creates the possibility of multiple, Pareto-ordered equilibria. In the optimistic equilibrium, warranties have value and firms have an incentive to remain in the market while, in the pessimistic equilibrium, consumers do not value warranties, choose not to buy from the firm, and thereby induce exit. These possibilities are examined for alternative market structures. In addition, we consider the government's role in influencing the selection of an equilibrium.

**Birge, John R.**

PD July 1987. TI Bounding the Expectation of Convex Functions with Limited Distribution Information. AU Birge, John R.; Dula, Jose H. AA Birge: University of Michigan. Dula: CORE. SR Universite Catholique de Louvain CORE Discussion Paper: 8733; Universite Catholique de Louvain Voie du Roman Pays, 34, B-1348 Louvain-la-Nueve BELGIUM. PG 21. PR No Charge. JE 215. KW Integration. Stochastic Programming. Moment Problem. Duality. Limited Information. Convex Functions. AB This paper considers bounds on the expectation of a convex function of a random variable when "only limited" information is available about the underlying distribution. The problem is presented as a generalized moment problem. A special class of functions is shown to have an easily computable solution to this problem with first and second moment constraints. Extensions are given for general convex functions on finite intervals or with finitely valued recession functions.

**Blackburn, Keith**


AB A stylized analytical model of two interdependent countries is used to examine game aspects of international macroeconomic policy design. The dominant theme centers on credibility problems arising from intrinsic uncertainty and the incentive for players to conceal or misrepresent private information in order to disguise their intention to export inflation abroad. By focusing on the precise incentive structure which motivates secrecy, together with the design of enforcement mechanisms for punishing such behavior, separating and pooling equilibria are identified which explicate conditions under which private information is revealed. These equilibria describe the state of inflation, output and the exchange rate and indicate circumstances under which either or both countries may experience a recession from non-cooperative behavior. Implications are drawn for cooperative decision making, emphasizing the dual role of cooperation in terms of both policy coordination and information coordination. This framework also demonstrates how various independent research can be viewed collectively within a single general paradigm.

**Blanchard, Olivier J.**

PD June 1987. TI Why Does Money Affect Output? A Survey. AA Massachusetts Institute of Technology. SR Massachusetts Institute of Technology Department of Economics Working Paper: 453; Department of Economics, Massachusetts Institute of Technology, Cambridge, MA 02139. PG 83. PR No Charge. JE 311, 023. KW Money Supply. Monetary Policy. Prices. Neutrality. Price Rigidity. AB Much of the research on economic fluctuations has focused on the effects on nominal money on output. This is not because money is the major source of movements in output: it is not. Rather, it is because economic theory does not lead us to expect such effects. Indeed it holds that, with flexible prices, money should be approximately neutral, with changes in nominal money being reflected in nominal prices rather than in output. Of course we know that, even with competitive markets, full information and flexible prices, the neutrality proposition is only an approximation. Any anticipated change in nominal money must lead to anticipated changes in the price level, and thus introduces a wedge between the opportunity cost of holding money and the cost of capital; in all cases this will affect utility and, in most cases, is likely to affect capital accumulation as well (see Fischer '1979 and Chapter 8). Even unanticipated changes, if they are the result of open market operations are likely to be non-neutral: open market transactions will usually involve some but not all...
holders of money and have distribution effects (see Rotemberg '1984, Grossman and Weiss '1983). But, except for the effects of steady inflation which may be substantial (especially when the non neutrality of the tax system is taken into account), these effects are mere intellectual curiosities; they can account neither for the size nor for the shape of the effect of money on output which we shall review below. For that reason, most of the research has taken as a given that prices do not adjust fully and instantaneously to nominal money and focused on the reasons for and implications of imperfect price adjustment. This will also be the approach of this survey.

Blomstrom, Magnus
PD September 1987. TI U.S. and Swedish Direct Investment and Exports. AU Blomstrom, Magnus; Lipsy, Robert E.; Kulchycky, Ksenia. AA Blomstrom and Lipsy: National Bureau of Economic Research. Kulchycky: University of Pennsylvania. SR National Bureau of Economic Research Working Paper: 2590; National Bureau of Economic Research, 1050 Massachusetts Avenue, Cambridge, MA 02138. PR $2.00. JE 431, 442, 411. KW Sweden. United States. Exports. Foreign Operations. AB Overseas production in a country by affiliates of Swedish and United States firms rarely appears to displace exports from the two home countries and in most cases either has no effect or tends to increase home country exports. The positive effect on Swedish exports is evident not only with respect to levels of exports to different countries at one time but also with respect to changes in exports over time. The positive effect on United States exports can be observed for minority-owned as well as majority-owned foreign operations.

Bloom, David E.
PD August 1987. TI Arbitrator Behavior in Public Sector Wage Disputes. AA Columbia University. SR National Bureau of Economic Research Working Paper: 2551; National Bureau of Economic Research, 1050 Massachusetts Avenue, Cambridge, MA 02138. PR $2.00. JE 831, 833, 026. KW Labor. Unions. Wages. Arbitration. Negotiation. Labor Disputes. Compromise. Bargaining. AB This study analyzes a new set of data on the decisions of conventional arbitrators. The main goal is to draw inferences about the extent to which conventional arbitration decisions are fashioned as mechanical compromises of the parties' final offers, without reference to the exogenous facts involved in different disputes. The results of the analysis are remarkably clear: conventional arbitrators tend to split the difference between the parties' final offers with virtually no evidence of additional systematic reference to the facts of the cases. However, since there is a substantial amount of unexplained variation in the arbitration decisions, this evidence of mechanical compromise behavior should be viewed as characterizing the overall operation of conventional arbitration mechanisms and not the behavior of individual arbitrators in any particular case. Indeed, the results are consistent with the view that individual arbitrators pay close attention to the facts of the cases, but that there is considerable variation in the structure of different arbitrators' preference functions.

Boadway, Robin
PD May 1987. TI Ex Post Versus Ex Ante Optimal Policies for Risky Activities. AU Boadway, Robin W.; Wildasin, David E. AA Boadway: Queen's University and CORE. Wildasin: Indiana University and CORE. SR Universite Catholique de Louvain CORE Discussion Paper: #501; Department of Political Economy, Johns Hopkins University, Baltimore, Maryland 21218. PG 36. PR No Charge. JE 321, 323, 023. KW Information. Efficient Markets. Heterogeneous Opinions. AB If traders with the same information reach different conclusions about an asset's value, the usefulness of price as a signal of private information is likely to be impaired. Traders may not be able to disentangle the differing information of others from their differing opinions. A general model of opinions and information is presented, in which opinions differ because different weights are applied to a set of unbiased signals. A simple example shows how the information value of price decreases as uncertainty about opinions increases. A slightly more complex case considers a market where a small number of traders have accurate inside information. A modified model is used to examine the effect of heterogenous opinions in the market for "lemons".

Boadway, Robin
PD November 1987. TI Economic Development and the Timing and Components of Population Growth. AU Bloom, David E.; Freeman, Richard B. AA Bloom: Columbia University. Freeman: Harvard University. SR National Bureau of Economic Research Working Paper: 2448; National Bureau of Economic Research, 1050 Massachusetts Avenue, Cambridge, MA 02138. PR $2.00. JE 112, 121. KW Economic Growth. Developing Countries. Productivity. Population Growth. AB This paper examines the relationship between population growth and economic growth in developing countries from 1965 to 1985. Our results indicate that developing countries were able to shift their labor force from low-productivity agriculture to the higher-productivity industry and service sectors, and to increase productivity within those sectors, despite the rapid growth of their populations. We also find that at given rates of population growth, income growth is related to the time path of population growth and that population growth due to high birth and death rates is associated with slower income growth than population growth due to relatively low birth and death rates. Hence, the timing and components of population growth are important elements in the process of economic development.
when random shocks affect particular industries, occupations, or regions. Workers can freely choose an industry or occupation ex ante, and can relocate, but only at a cost, once uncertainty is resolved. The policy instruments available to the government are per capita taxes and subsidies. These are chosen either to maximize ex post utilitarian aggregate welfare, treating the initial assignment of workers as exogenously fixed (ex post optimal policy), or to maximize the ex ante expected utility of a representative worker, taking the effect of policy choice on the ex ante allocation of labor into account (ex ante optimal). Ex ante and ex post optimal policies are compared, with or without institutional constraints on the set of instruments. Optimal policies range from complete equalization of net incomes across workers to no equalizing transfers at all depending on the instruments available and the nature of relocation costs.  

Bonanno, Giacomo  

AB The logical structure of rational play in extensive games is investigated. Players are assumed to share a common method of reasoning which is represented by the language of propositional logic, applied to a set of propositions containing a definition of individual rationality and a description of the game. A definition of rational solution is suggested and it is shown that rational solutions need not be Nash equilibria. Particular attention is paid to the logical basis for "rational" plans concerning unreached parts of the game tree.

Bordo, Michael D.  
PD August 1987. TI The ECU--An Imaginary or economy's capital stock as state variable. We try to investigate the dependence of the resulting optimal dynamics on the value of the discount factor and on the structure of the two-sector technology. We show not only that "everything can happen" in a neoclassical competitive equilibrium, but we also supplement some reasonable economy conditions which assure regular behaviors and others, equally acceptable from the standpoint of economic theory, which implies instead chaotic optimal paths. The interplay between the level of discounting and the relative capital/labor intensity of the two sectors is proved to be the critical element.
Embryonic Form of Money: What Can We Learn from History?  
AU Bordo, Michael D.; Schwartz, Anna J.  
AB We present historical examples of new forms of money that can be compared with the European Currency Unit. We first define the ECU in its official role before turning to developments in the private market for ECUs. We then examine historical antecedents of three attributes of ECUs: a unit of account; a basket of currencies; a basis for monetary integration. We discuss which features if any of ECUs are unique, and the contribution of the historical analysis to assessing the future of ECUs. We then ask whether governments or markets have been dominant in the emergence of new forms of money. Whatever emerges as money in an economy becomes the general means of payment. Prices of commodities, services, and bonds are expressed in units of the money. Buyers use the money to purchase goods or bonds and sellers receive the money in exchange for goods or bonds. We conclude that, at this stage in its history, the ECU at best is an embryonic form of money, closer to historical imaginary monies than to existing currencies that the world has known.  
PD November 1987. TI Credible Commitment and Exchange Rate Stability: Canada’s Interwar Experience.  
AB In January 1929 the Canadian government suspended gold exports and began a floating exchange rate regime that endured until the onset of World War II. In sharp contrast with the experience of other countries which left the gold standard, deflation and declining economic activity continued in Canada until 1933. This paper examines the determinants of the Canadian exchange rate in the 1930’s and provides an answer to the question of why the Canadian dollar did not depreciate in the early 1930’s despite Canada’s de facto departure from the Gold Standard. We develop the answer in two stages. First, we show that the government made a clear commitment to maintain a contractionary monetary policy. It did so because it believed: that monetary expansion would increase the value of external obligations without reducing the value of domestic obligations; and that even if all contractual obligations were met, Canada would lose her reputation as a responsible debtor. Second, we argue that the government’s commitment was viewed by the public as credible. The credible commitment dominated market agent’s expectations of the evolution of the exchange rate.  
Borsch, Supan Axel  
PD August 1987. TI Household Dissolution and the Choice of Alternative Living Arrangements Among Elderly Americans.  
AB For the elderly, housing choices are more complex than merely the choice of housing expenditure, dwelling size, and tenure. They also include the choice among alternative living arrangements such as living in one household with their adult children or sharing accommodations with other related or unrelated elderly. We first contrast living arrangements of elderly Americans with the population under age 65 and describe the changes from 1974 to 1983. We detect a growing discrepancy in household formation/dissolution patterns between the elderly and the younger population: after a steady decline in the 1970s, we observe a rapid increase in the rate of “doubled-up” young families in the beginning of the 1980s. No such development can be found among elderly Canadians. Instead, the proportion of elderly living independently steadily increases from 1974 to 1983. To explain this discrepancy, we estimate a multinomial choice model among living independently and six categories of alternative living arrangements. The main finding is the predominance of demographic determinants as opposed to economic variables. The difference in income growth between the young and the elderly — real income declined for the young but increased for the elderly — can explain only part of the discrepancy in household dissolution decisions. The remaining discrepancy must be attributed to inertia and low mobility rates.  
Bos, Dieter  
AU Bos, Dieter; Tillmann, Georg. AA University of Bonn. SR Universitat Bonn Sonderforschungsbereich 303 - Discussion Paper: A-145; Sonderforschungsbereich 303 an der Universitat Bonn, Adenauerallee 24-42, D-5300 Bonn 1, DEUTSCHLAND.  
AB This paper presents a positive theory of privatization. No welfare arguments enter the analysis. The government is conceived as an institution which wants to draw some money from selling its property and so willingly cooperates with private shareholders who also are interested in the value of the firm. The paper is organized as follows. In section 2 we present the actors of our model and describe their objectives. Then, in section 3, the two-tier optimization approach is described, where tier one is the privatization game and tier two is the adjustment
game in the firm. In section 4 we derive the results of the tier-one game: what is the optimum extent of privatization, and of employees' shares? In section 5 we derive the results of the tier-two game: when does the trade union's interest in keeping jobs lead to inefficient production, what are the optimal input and pricing policies?

Boskin, Michael J.
AB This paper presents new updated and improved estimates of various components of governments' contribution to national wealth and its growth in the post-war period. The primary conclusions drawn are: 1. The federal government's assets, tangible and financial, are substantial; they grew more rapidly than the national debt in the 1970s. 2. Since 1980, conventional liabilities have grown much faster than assets, causing about a $727 billion decline in federal "net worth"; 3. The state-local government sector contributes importantly to government and national wealth. 4. Total government reproducible capital was about 55 per cent of the corresponding private non-residential capital stock in 1985; 5. Government net investment has often been sufficient to turn the government sector into a net saver despite large budget deficits; 6. Extending the traditional National Income Accounts to include imputed returns to government capital and consumer durables while treating government net investment and durable purchases as saving indicate that the share of national output devoted to consumption has risen substantially, while that devoted to net saving has fallen sharply in the period 1951-85. 7. The inclusion of consumer durables and government tangible investment raises the national saving rate substantially. Thus, the data presented in this paper reveal much about the post-war fiscal history of the United States. In addition to their importance in understanding trends in national wealth, they may also prove important inputs into future studies of the long-term growth of the economy and to the short-run effects of fiscal policy.

Bronsard, Camile
TI Roy-Consistent Expectations. AU Allard, Marie; Bronsard, Camile; Richelle, Yves.

Buchner, Heinz Jurgen

Buitr, Willem
AB The paper provides an account of the current global economic situation, outlook and policy options. Medium-term prospects are mediocre and fraught with considerable downside risk. Fiscal and monetary policy options for the main industrial countries to improve global economic performance are outlined. The worries about the United States fiscal position are shown to be exaggerated. It is also argued that while the United States economy is well on course to become a net external debtor, it has not yet reached that position. In the longer run, prosperity or depression will be determined to a large extent by policy choices.

Burgess, Simon M.

AB This paper presents a procedure to estimate intertemporal dynamic decision rules where adjustment costs are assumed to be variable. The estimation is based on the Euler equation. For purposes of illustration we concentrate on an employment function for U.K. manufacturing sector where we find very significant effects of some variables which influence adjustment costs. Finally, we point out an empirical result which has interesting implications when evaluating tests of 'efficient bargain' models.

Campbell, John Y.

AB This paper reexamines the consistency of the permanent income hypothesis with aggregate, post-war, United States data. The permanent income hypothesis is nested within a more general model in which a fraction of income accrues to individuals who consume their current income rather than their permanent income. This fraction is estimated to be 40 or 50 percent, indicating a substantial departure from the permanent income hypothesis. This finding is robust to various statistical problems that have plagued previous work, such as time aggregation, and cannot be easily explained by appealing to changes in the real interest rate or to non-separabilities in the utility function.

Case, Karl E.

AB This paper uses data on nearly a million homes sold in four metropolitan areas -- Atlanta, Chicago, Dallas and San Francisco -- to construct quarterly indexes of existing home prices between 1970 and 1986. We propose and apply a new method of constructing such indexes which we call the weighted repeat sales method (WRS). We believe the results give an accurate picture of the actual rate of appreciation in home prices in the four cities. The paper explains the construction of the index, discusses the results and compares them with the National Association of Realtors data on the median price of existing single family homes for the period 1981-1986.

Cave, J. A. K.

AB This paper applies several refinements of sequential equilibrium to a signaling game of legal settlement, in which the informed plaintiff has a continuum of pure strategies. The principal results are that (1) such refinements can greatly reduce the scope of equilibrium behavior; (2) there is no necessary connection between divine and perfect equilibria; and (3) perfect, divine, and proper equilibria of games with continuous pure strategy spaces may use weakly dominated strategies with positive probability.
ABSTRACTS


AB This paper analyses voting situations where individual preferences need not be single-peaked, but satisfy a hierarchical ordinal equivalence condition. Such preferences arise in marketing boards and models of pollution abatement. The ideal point of the median voter is the unique Condorcet winner, and it is immune to manipulation.

Cecchetti, Stephen G.


AB This paper describes how to value the exchange provision and correct the measurement of the yields of traded securities. These are then used to construct estimates of the term structure of nominal interest rates monthly from 1929 to 1949. These new data replace the sketchy data contained in the Federal Reserve Board's Banking and Monetary Statistics of the United States, and for the first time allow one to follow changes in the shape of the term structure. The interest rate data can be added to new data on three and six month time loans in Mankiw and Miron(1986) and the new output, production and unemployment data in Romer (1986a, 1986b, 1986c and 1987). The remainder of this paper is divided into five sections. Section II provides a discussion of the raw data that were collected and used to estimate the yield curves. This is followed by an explanation of how the exchange provision was valued and used to correct the apparent negative nominal yields. Section IV examines the tax status of various securities. The following section describes the estimation of the yield curves, which uses a technique derived by Nelson and Siegel (1985) and presents the estimates themselves.

Chaiken, Jan M.

TI Identifying High-Rate Serious Criminals from Official Records. AU Rolph, John E.; Chaiken, Jan M.

Chaloupka, Frank

TI Nutrition and Infant Health in Japan. AU Yamada, Tadashi; Yamada, Tetsuji; Chaloupka, Frank.

Cheng, Harrison H. C.


AB A general existence result for competitive equilibrium in asset markets with short sales is obtained. The number of assets may be infinite. The commodity space can be any Hausdorff locally convex topological vector space. Two important assumptions are: (1) there exists an open convex cone of arbitrage, (2) the set of all individually rational attainable allocations is weakly compact.

Clark, Robert L.

TI Pension Wealth, Age-Wealth Profiles, and the Distribution of Net Worth. AU McDermid, Ann; Clark, Robert L.; Allen, Steven G.

Colbourn, Charles J.


AB A matroid Steiner problem is obtained by selecting a suitable subfamily C of the cocircuits, and then defining a Steiner "tree" to be a minimal set having nonempty intersection with all members of C. The family of all sets whose complements contain Steiner trees forms an independence system which we call the Steiner complex. We show that this Steiner complex can be partitioned into as many intervals as there are bases in the underlying matroid. As a special case, we obtain explicit partitions of the independent sets of any matroid. It also shows that both F-complexes arriving in network reliability problems and the family of bipartite subgraphs of a graph can be partitioned into as many intervals as there are spanning trees. We also describe a generalization of the Tutte polynomial for matroids to an extended Tutte polynomial for Steiner complexes. This provides an alternative method for evaluating the independence or reliability polynomial. We also discuss applications to network reliability.

Cook, W.


AB Chvatal introduced the idea of viewing cutting planes as a system for proving that every integral solution of a given set of linear inequalities satisfies another given
linear inequality. This viewpoint has proven to be very useful in many studies of combinatorial and integer programming problems. The basic ingredient in these cutting-plane proofs is that for a polyhedron \( P \) and integral vector \( w \), if \( \max \{ wx | x \in P \} \leq t \), then \( wx \leq t \) is valid for all integral vectors \( x \) in \( P \). We consider the variant of this step where the requirement that \( wx \) be integer may be replaced by the requirement that \( w(\bar{x})x \) be integer for some other integral vector \( w(\bar{x}) \). The cutting-plane proofs thus obtained may be seen either as an abstraction of Gomory's mixed integer cutting-plane technique or as a proof version of a simple class of the disjunctive cutting planes studied by Balas and Jeroslow. Our main result is that for a given polyhedron \( P \), the set of vectors that satisfy every cutting plane for \( P \) is again a polyhedron. This allows us to obtain a finite recursive procedure for generating the integer hull of a polyhedron, analogous to the process of repeatedly taking Chvátal closures in the integer programming case. These results are illustrated with a number of examples from combinatorial optimisation. Our work can be seen as a continuation of that of Nemhauser and Wolsey on mixed integer cutting planes.

Cooper, Russell


AB This paper investigates the dynamic behavior of an economy with multiple Nash equilibria. The first part of the paper analyzes an abstract game exhibiting multiple equilibria. A history dependent selection criterion is proposed which induces correlated behavior in equilibrium even though agents are playing one-shot games and disturbances are not correlated over time. The second part of the paper investigates a specific model of multiple equilibria. Here the multiplicity is induced by the presence of a discrete decision on the part of firms regarding their choice of technique. The implications of the selection criterion introduced in the first part of the paper are illustrated through this example. Again correlated behavior emerges in a sequence of independent one-shot games. The model economy may also experience prolonged periods in which a low productivity technology is in use and then, as a consequence of a large real disturbance, may switch to an alternative equilibrium in which a high productivity technology is utilized. The paper also discusses the Pareto ordering of these equilibria.


AB This paper studies the dynamic properties of an imperfectly competitive economy with inventory holdings. In particular, we focus on the serial correlation in aggregate output and employment produced by the holding of inventories in one sector of the economy and the co-movement between sectors of an economy over the cycle resulting from demand linkages. This model is then contrasted with a simple, competitive real business cycle model with inventories. We find that the predictions of these models with regards to the co-movement of employment may differ. Based on this, we present empirical evidence on the co-movement of employment over the business cycle which is consistent with the predictions of the model of imperfect competition with inventory holdings and demand linkages.

TI Warranties Without Commitment to Market Participation. AU Bigelow, John; Cooper, Russell; Ross, Thomas W.

AB This paper studies the dynamic properties of an imperfectly competitive economy with inventory holdings. In particular, we focus on the serial correlation in aggregate output and employment produced by the holding of inventories in one sector of the economy and the co-movement between sectors of an economy over the cycle resulting from demand linkages. This is then contrasted with a simple, competitive real business cycle model with inventories. We find that the predictions of these models with regards to the co-movement of employment may differ. Based on this, we present empirical evidence of the co-movement of employment over the business cycle which is consistent with the predictions of the model of imperfect competition with inventory holdings and demand linkages.

Corman, Hope


AB This study compares the cost-effectiveness of various health inputs and government programs in reducing race-specific neonatal mortality or death in the first twenty-seven days of life. Approximately two-thirds of all infant deaths occur within this time period. The programs and
inputs at issue are teenage family planning use, the supplemental food program for women, infants and children (WIC), use of community health centers and maternal and infant care projects, abortion, prenatal care, and neonatal intensive care. Using an economic model of the family as the analytical framework, effectiveness is determined by using ordinary least squares and two-stage least squares to estimate infant health production functions across large counties in the United States in 1977. Estimates of costs are from a number of published sources. We find the early initiation of prenatal care to be the most cost-effective means of reducing the neonatal mortality rate for black and whites. Moreover, blacks benefit more per dollar of input use than whites. Neonatal intensive care, although the most effective means of reducing neonatal mortality rates, is one of the least cost-effective strategies.

Cornet, Bernard

AB We show that in a general equilibrium model with 1 goods and n firms with (possibly) nonconvex production sets, the so-called survival assumption, along with standard assumptions, implies that the set of (resp. efficient) attainable production plans is homeomorphic to the closed unit ball of R([ln]')resp.R'([-1],n).

Cornwell, Christopher

AB In panel data models with fixed effects, the maximum likelihood estimator (MLE) is generally inconsistent, because the number of parameters increases with sample size. A common solution is to condition on sufficient statistics for the effects. The conditional maximum likelihood estimator (CMLE) maximizes the resulting conditional likelihood and is generally consistent. In the linear regression model, however, the MLE is consistent and in fact coincides with the CMLE. We extend this result to the simultaneous equations model, and we allow exogenous variables other than the intercept to have individually-varying coefficients, so long as the set of such variables is the same in each equation.

Coullard, Colette

AB The cycle polytope of a graph is the convex hull of the incidence vectors of the cycles of the graph. In this paper we provide a complete linear defining system for the cycle polytope for Halin graphs. In addition, we give a short proof of Seymour's characterization of the cone generated by the incidence vectors of cycles for an arbitrary graph.

Courakis, Anthony S.

AB In the last fifteen years a considerable empirical literature has been amassed that ventures to account for the sectoral pattern of trade of various economies, in terms of a model that distinguishes between three factors of production - notably physical capital, labour, and human capital. Relative to alternative specifications that either abstract from human capital, or aggregate human capital with physical capital, or allow for the quality composition of the labour force by distinguishing between groups of different levels of skill, such a model is claimed to have both conceptual and empirical merit. The discussion in this paper questions the wisdom of relying a priori on econometric specifications that involve the constraint that the effect of human capital on trade performance is independent of the composition of human capital. It is stressed that, in a setting devoid of any precise analytical reasoning that will sustain such a premise, this type of specification comprises an inefficient modelling procedure that will often imply that information within our reach and consistent with the neo-factor proportions paradigm is not accessed and may even result in erroneous inferences about a country's pattern of comparative advantage.

Cowell, Frank A.

AB We examine the effect of random tax enforcement in a simplified model of public goods supply. Individuals who might actually like an increase in the public good supply at the expense of their own private consumption will, nevertheless, want to opt out of paying their share of the required taxes: but if they evade some portion of their
taxes they may be caught and penalised. The responsiveness of taxpayers to tax and enforcement parameters is shown to depend critically on the extent of provision of publicly supplied goods and the "publicness" of these goods in terms of their non-rivalness and non-excludability. In particular the model has interesting implications for the effects on the size of the black economy of the size of the public sector, the type of public good supplied, and the degree of conformity between taxpayers.

Crane, Keith
AB This report provides military expenditure estimates for the Northern Tier countries of the Warsaw Pact (Czechoslovakia, the German Democratic Republic, and Poland) and Hungary, assesses the political and economic factors that determine these spending levels, and discusses the probable course of military spending in these countries over the next several years. These estimates suggest that the defense budgets reported by the East Europeans contain most major components of military spending. A statistical analysis of factors that may determine military spending levels indicates the primary determinant is available resources -- i.e., utilized national income. The prospects for large surges in military spending in the next few years are therefore low.

Cumby, Robert
AB In this paper we present a model of a balance-of-payments crisis and use it to examine the Argentine experiment with a crawling peg between December 1978 and February 1981. The approach taken allows us to examine the evolution of a crisis when the collapse is not a perfectly-foreseen event. The implementation of the model yields plausible values of the one-month ahead probabilities of a collapse of the crawling peg. The probabilities exhibit a sharp increase in the middle of 1980 and indicate a significant loss of credibility throughout the remainder of the year. The results suggest that viability of an exchange rate regime depends strongly on the domestic credit policy followed by the authorities. If this policy is not consistent with the exchange rate policy pursued by the authorities, confidence in the exchange rate policy is undermined.

AB The paper examines if real stock returns in four countries are consistent with consumption-based models of international asset pricing. The paper finds that ex-ante real stock returns exhibit statistically significant fluctuations over time and that these fluctuations cannot be explained by consumption-based models when the conditional covariances between real stock returns and the rate of change of consumption are assumed to be constant over time. These conditional covariances are then modeled and the paper finds that they too exhibit statistically significant fluctuations over time. However, even when conditional covariances are allowed to change over time, the paper finds that the consumption-based models do not fully explain real stock returns.

Crane, Keith
AB This paper analyzes ex-ante returns to forward speculation and asks if these returns can be explained by models of a foreign exchange risk premium. After presenting evidence that both nominal and real expected speculative profits are non-zero, the paper examines if real returns to forward speculation are consistent with consumption-based models of risk premia. Estimates of the conditional covariance between real speculative returns and real consumption growth are presented and, like ex-ante returns to forward speculation, they exhibit statistically significant fluctuations over time and often change sign.

Danchick, Roy
TI Air Force Academy Attrition: A New Perspective on the College Dropout Problem. AU Salant, Stephen W.; Danchick, Roy.

DAspremont, Claude
AB A two-stage duopoly where firms choose first R&D expenditures and then production levels is analyzed under various types of agreements. It is seen that, in terms of welfare, cooperative behavior can play a positive role when R&D activities generate spillover effects.

Davidson, Carl
PD September 1987. TI Optimal Labor Market Policies with Search Unemployment. AU Davidson, Carl; Martin, Lawrence; Matusz, Steven.
In this paper, we analyze a two sector general equilibrium model that allows for a positive level of unemployment unemployment. Unemployment arises due to frictions in the labor market that keep firms and workers from finding each other immediately. The types of frictions encountered in the two sectors are assumed to be different so that the level and structure of unemployment varies across sectors. We demonstrate that, under certain assumptions about the search technology, the economy operates along its static production possibilities frontier. It will not, however, produce the allocation that maximizes the utility from instantaneous consumption. In fact, the economy produces too little of the good produced in the sector with high unemployment. We show that unemployment compensation is an effective way to transfer resources to the desired sector, and therefore improve static efficiency. On the other hand, we also demonstrate that due to the fact that the structure of unemployment differs across sectors, the economy produces too many jobs of low value. We discuss labor market policies that would be helpful in ameliorating this problem and explain why the durability of a job is important. In particular, we show that the durability of a job is an important element of its dynamic social value.

Davidson, Russell
PD July 1987. TI Double-Length Artificial Regressions. AU Davidson, Russell; MacKinnon, James. AA Queen's University. SR Queen's Institute for Economic Research Discussion Paper: 691; Department of Economics, Queen's University, Kingston, Ontario, Canada K7L 3N6. PG 22. PR $3.00 Canada; $3.50 United States and Foreign. JE 211. KW Gauss-Newton Regression. Specification Tests. Maximum Likelihood. Functional Form. Nonlinear Regression. AB Artificial linear regressions often provide a convenient way to calculate test statistics and estimated covariance matrices. This paper discusses one family of these regressions, called "double-length" because the number of "observations" in the artificial regression is twice the actual number of observations. These double-length regressions can be useful in a wide variety of situations. They are quite easy to calculate, and seem to have good properties when applied to samples of modest size. We first discuss how they are related to the more familiar Gauss-Newton and squared-residuals regressions for nonlinear regression models, then show how they may be used to test for functional form, and finally discuss several other ways in which they may be useful in applied econometric work.

TI Testing for Consistency Using Artificial Regressions. AU MacKinnon, James G.; Davidson, Russell.

Davis, Carolyn D.
PD August 1987. TI Stock Market Volatility. AU Davis, Carolyn D.; White, Alice P. AA Board of Governors of the Federal Reserve. SR Board of Governors of the Federal Reserve System Staff Studies Paper: 153; Staff Studies Section, Division of Research and Statistics, Board of Governors of the Federal Reserve System, Washington, DC 20551. PG 14. PR No Charge. JE 313, 311. KW Stock Market. Stock Prices. New York Stock Exchange. Financial Instruments. Trading Innovations. Volatility. AB This study reviews innovative strategies in stock trading and examines several aspects of share price volatility to determine whether there has been a measurable change in recent years. The empirical review cannot appraise the volatility associated with specific trading innovations but rather looks at changes in underlying volatility. It also does not directly address intraday volatility because transactions prices, other than those for the last transactions of each day, are not readily available. The first section reviews the institutional factors that are believed to be affecting stock price volatility, and the second section examines the volatility itself. The concluding section surveys changing economic and financial conditions as potential sources of the observed volatility of stock prices.

Day, Richard H.
PD September 1987. TI Economic Development in the Very Long Run. AA University of Southern California. SR University of Southern California Modelling Research Group Working Paper: M8732; Department of Economics, University of Southern California, University Park, Los Angeles, CA 90089-0152. PG 46. PR No Charge. JE 023, 112, 113. KW Complex Dynamics. Regime Switching. Infrastructure. AB This paper is concerned with epochal economic change. A sufficiently great population facilitates an enlarged infrastructure which in turn makes possible a new regime with improved productivity and modified mortality. Continued growth within a given regime eventually depresses productivity; as population expands internal and external pressures create the conditions for a possible transition. Irregular fluctuations with reswitching may occur prior to an escape to a new age. Development in the very long run is thus a multiple phase process involving the switching of regimes brought about by intrinsic demoeconomic forces.

de Janvry, Alain
PD June 1987. TI Agrarian Structure, Technological Innovations, and the State. AU de Janvry, Alain; Sadoulet, Elisabeth; Fafchamps, Marcel. AA Department of Agricultural and Resource Economics, University of California, Berkeley. SR University of California at Berkeley Department of Agricultural and Resource Economics (CUDARE) Working Paper: 442; 207 Giannini Hall, University of California, Berkeley, CA. PG 51. PR $10.20. JE 021, 711, 712. KW Technological Change. Innovations. Agriculture. Induced Innovations. Technological Bias. AB A major advance was made with the theory of
induced technological innovations which uses price signals to explain rate and bias. We start by reviewing the achievements of this theory to conclude that price signals are indeed a necessary but far from sufficient explanation. Using a transactions cost approach in a context of incomplete markets, we show that the structure of asset ownership is also an important determinant of the rate and bias of technological change. Finally, when technology is a public good generated in public research institutions, collective action can be used to affect the allocation of resources to alternative technological innovations. The structure of political power can thus further distort the rate and bias of technological change. We use a formal model of optimum technological choice to show in what direction structural characteristics of agriculture and collective action affect the bias of technological change. We also use cross-country data to show that structural characteristics and the size of public research budgets do indeed affect the nature of technological change beyond the effect of price signals.


AB The less-developed countries (LDCs) have been the fastest growing source of demand for United States agricultural exports during the last two decades. This is particularly true for food grains in the lower income LDCs and for feed grains in the upper income LDCs. Among these countries, it is those with the highest economic growth performance which have also been the ones with the highest growth in import demand. The performance of United States agricultural exports has thus been inextricably tied to the economic performance of the LDCs, and this is even more likely to be the case in the future.


AB The debt crisis that started in 1982 forced the Latin American countries to implement drastic stabilization policies and structural adjustment programs. The consequent depreciation of the real exchange rate has transformed agriculture into the relatively most dynamic sector of the economy. This creates the possibility of defining a forward looking rural development strategy that is consistent with this new role for agriculture and that has the potential of significantly lessening rural poverty. Starting from a social poverty map for the rural areas, we identify a five pronged approach that includes: (1) farm-oriented rural development projects for the upper subfamily and family farms; (2) household-oriented rural development projects for the lower subfamily farms; (3) access to additional assets for the landless and subfamily farmers through land reform and colonization; (4) employment creation and labor market rationalization; and (5) the promotion of backward, forward, and final demand linkages with agriculture located in the rural areas.

de Pablo, Juan Carlo

TI Argentina: Debt and Macroeconomic Instability. AU Dornbusch, Rudiger; de Pablo, Juan Carlo.

de Palma, Andre

TI Bottleneck Congestion with Elastic Demand. AU Arnott, Richard; de Palma, Andre; Lindsey, Robin.

DeMarzo, Peter


AB The Modigliani-Miller Theorem is shown to hold in a general model of a multi-period stochastic economy with incomplete markets. In the model, firms are allowed to trade available securities, including shares of other firms. Thus, share prices and dividends become fully interdependent in general. However, it is demonstrated that changes in firm financial policy in no way alters equilibrium allocations or prices. This is done by establishing that agents are able to adjust their own portfolios and neutralize corporate policy.

DePalma, Andre

TI Spatial Price Policies and Duopoly. AU Anderson, Simon P.; DePalma, Andre; Thisse, Jaques Francois.

Dewatripont, Mathias


AB This paper uses a computable general equilibrium model...
model of Turkey to explore the empirical effect on adjustment to various macroeconomic shocks of a variety of "structuralist" rigidities. Four types of rigidities are considered: exchange rate rigidity leading to premium rationing and rent seeking, wage rigidities leading to unemployment or labor scarcity, investment-savings imbalance leading to rationing of private consumption — forced saving — or to overall Keynesian unemployment, and sectoral price rigidity leading to consumption or supply rationing. In a series of comparative statics experiments, we explore the impact of, and interactions among, these different types of rigidities. In general, the results indicate that interaction effects are very important, especially between the macro closure rule, which specifies how investment-savings balance is achieved, and the other rigidities. Price rigidities are most damaging when a shock necessitates large relative price changes in a Walrasian world. Also, price rigidities are much more harmful when they lead to situations of excess supply rather than excess demand.

Dickens, William T.

PD August 1987. TI Employee Crime, Monitoring and the Efficiency Wage Hypothesis. AU Dickens, William T.; Katz, Lawrence; Lang, Kevin; Summers, Lawrence. AA Dickens: University of California, Berkeley. Katz and Summers: Harvard University. Lang: Boston University. SR National Bureau of Economic Research Working Paper: 2356; National Bureau of Economic Research, 1050 Massachusetts Avenue, Cambridge, MA 02138. PR $2.00. JE 916, 512, 513, 821. KW Crime. Bonding. Efficiency Wages. Employee. AB This paper offers some observations on employee crime, economic theories of crime, limits on bonding, and the efficiency wage hypothesis. We demonstrate that the simplest economic theories of crime predict that profit-maximising firms should follow strategies of minimal monitoring and large penalties for employee crime. Finding overwhelming empirical evidence that firms expend considerable resources trying to detect employee malfeasance and do not impose extremely large penalties, we investigate a number of possible reasons why the simple model's predictions fail. It turns out that plausible explanations for firms large outlays on monitoring of employees also justify the payment of premium wages in some circumstances. There is no legitimate a priori argument that firms should not pay efficiency wages once it is recognised that they expend significant resources on monitoring.

Dierker, Egbert

PD August 1987. TI Quantity Guided Price Setting. AU Dierker, Egbert; Neuefeind, Wilhelm. AA Dierker: University of Vienna. Neuefeind: Washington University in St. Louis. SR Universitat Bonn Sonderforschungsbereich 303 - Discussion Paper: A-129; Sonderforschungsbereich 303 an der Universitat Bonn, Adenauerallee 24-42, D-5300 Bonn 1, DEUTSCHLAND. PR No Charge. JE 021. KW Two Sector Economy. General Equilibrium. Planning Agency. Imperfect Competition. AB We consider an economy with two sectors. The first sector consists of competitively behaving consumers and producers; the second, non-competitive, sector, the P-sector, consists of firms (P-firms) producing commodities (P-goods) that are not produced in the competitive sector. The P-firms receive their gross output levels and the market prices of their inputs as decision parameters. They minimize costs and set prices for their outputs according to a specific pricing rule. There is also a planning agency that ensures that a certain net production (gross production minus the intra-consumption in the P-sector) of the P-goods is achieved. We give assumptions ensuring the existence of equilibrium which requires market clearing, meeting the production aspirations of the planning agency, and setting prices for the P-goods which are compatible with market prices in the sense that the market prices cannot be higher than the prices to be charged by the P-firms, and if the target for a P-good is exceeded, the price charged by the P-firm equals the market price.

PD October 1987. TI A Goodness of Fit Test of Dual Labor Market Theory. AU Dickens, William T.; Lang, Kevin. AA Dickens: University of California, Berkeley. Lang: Boston University. SR National Bureau of Economic Research Working Paper: 2350; National Bureau of Economic Research, 1050 Massachusetts Avenue, Cambridge, MA 02138. PR $2.00. JE 821, 212, 824. KW Labor Market. Wage Distribution. Wages. AB We subject our dual labor market model to a goodness of fit test and compare the results with those obtained using a single equation model with a complex error structure. The dual labor market does an excellent job of predicting the wage distribution except for failing to explain bunching at $7.50 and $10.00 per hour. The null hypothesis that the model is correct cannot be rejected at the .05 level. In contrast, the wage distribution predicted by the single labor market model differs significantly from the observed distribution.
Dolado, Juan J.
TI Intertemporal Rules with Variable Speed of Adjustment: An Application to U.K. Manufacturing Employment. AU Burgess, Simon M.; Dolado, Juan J.

Domingo, Lita
TI Change in the Status of Women Across Generations in Asia. AU King, Elizabeth; Peterson, Jane; Adioetomo, Sri M.; Domingo, Lita; Syed, Sabiha H.

Dornbusch, Rudiger
AB This paper investigates the role of interest rates, commodity prices, growth in bringing the debt crisis about and how they facilitated or made more difficult the first five years of adjustment. We also ask whether and how the world macroeconomy is likely to contribute to the solution of the debt problem in the next five years. The paper starts with a conceptual framework and a review of the behavior of key macroeconomic variables in the past quarter of a century. Next the origins of the debt crisis are discussed as well as the adjustment period, 1982-1987. The following part reviews alternative scenarios for the period 1987-90 and their bearing on debt questions. We also ask what contribution to expect from commercial policies. The paper concludes pessimistically that for many debtors there is not a sufficient improvement to be expected from good performance of the world economy.

Dornbusch, Rudiger
AB The paper reviews the Argentina debt experience in the past ten years. The emphasis is on the interaction between relative prices, financial instability, budget deficits, inflation and debt accumulation. A longer run perspective shows that the continuing fiscal problems have stood in the way of investment and growth.

Dreze, J.
TI Generic Inefficiency of Stock Market Equilibrium When Markets Are Incomplete. AU Geanakoplos, J.; Magill, M.; Quinsii, M.; Dreze, J.

Dula, Jose H.
AB We introduce an upper bound on the expectation of a special class of sublinear functions of multivariate random variables defined over the entire Euclidean space without an independence assumption. The bound can be evaluated easily requiring only the solution of systems of linear equations thus permitting implementations on high-dimensional space. Only knowledge on the underlying distribution means and second moments is necessary. We discuss pertinent techniques on dominating general sublinear functions by using simpler sublinear and polyhedral functions and second order quadratic functions.

Dymski, Gary A.
AB This paper develops a theory of the banking firm using a macrofoundation constructed from the work of Keynes, Davidson, and Minsky. This macrofoundation, which emphasizes the centrality of real time, institutional constraint, and disequilibrium adjustment, leads to a theory of banks as "two-sided" entities engaged in the dual roles of credit creation and liquidity provision. This two-sided or Keynesian model is consistent with the post Keynesian monetary framework. Further, this Keynesian banking model suggests two refinements in theory of financial fragility, a prominent part of the post Keynesian monetary framework: (1) it allows monetary contraction to be included among the causes of economic downturns; (2) it allows an explanation of why financial fragility leads to crisis in a downturn. Both suggested refinements stem directly from the special vulnerability implicit in banks' dual functions. Finally, empirical support based on data from the Terms of Lending Survey is provided for the Keynesian model developed herein.

Eaton, Jonathan
AB When rents generated by government policies are perceived as permanent, the rights to earn them may be capitalized as assets that form a component of nonhuman wealth. The existence of such assets raises international
indebtedness, while shifts in policy that increase or reduce the importance of such rents can generate movements in the current account that are correlated with the real exchange rate. Because the elimination of policies that generate rents imposes a capital loss that is born entirely by generations currently alive, while the benefit of the removal of a distortion is shared between those alive and unborn generations, a possibility is that such a reform can reduce the expected lifetime welfare of everyone alive. If a monopoly exists in the provision of nontraded goods then there may be several steady states that can be Pareto ranked.

Ebert, Udo

Eckstein, Z.

AB This paper provides an analysis of a university optimization problem that attempts to control quality and quantity of engineers. This problem is embedded within an equilibrium model that considers the dynamic rational occupation choice of high school graduates and the effect of the students and the university decision on the current and future demand and supply of engineers. The explicit considerations lead to an estimable model that is capable of providing economic forecasts on the demand and supply of electrical engineers under various economic conditions. Using aggregate data from Israel the model is estimated. The estimated parameters are consistent with the economic theory and the fit to the sample is very good. In particular, the model is capable of estimating the observed cyclical movements in the number of graduating electrical engineers in Israel. Finally, we provide several predictions on the equilibrium number of electrical engineers towards the end of the century.

Edwards, Sebastian

AB This paper deals with the anatomy of devaluation in Latin America. In an effort to understand the economics surrounding the causes and consequences of exchange rate crises, eighteen devaluation episodes that took place between 1962 and 1982 are investigated in detail. The paper focuses on: (1) the relation between (inconsistent) macroeconomics policies and exchange rate crises; (2) the role of real exchange rate overvaluation in the precipitation of balance of payment crises under predetermined nominal exchange rates; (3) the role of exchange controls, multiple exchange rates and black markets in the period preceding devaluations; and (4) the effectiveness of nominal devaluations as a way to restore real exchange rate equilibrium. A distinction is made between stepwise devaluations and crawling peg regime. It was found that historically most stepwise devaluations have had difficulty in sustaining a real devaluation over the medium term. Countries that adopted a crawling peg have generally been able to maintain a higher real exchange rate. In many cases, however, this has been achieved at the cost of substantial inflation.


AB In this paper we investigate the relation between tariff changes, terms of trade changes and the equilibrium real exchange rate. For this purpose we use two models of a small open economy: (1) a three goods version of the Ricardo-Viner model; and (2) a three goods model with full intersectoral factor mobility. We show that, in general, it is not possible to know how the equilibrium real exchange rate will respond to these two disturbances. Moreover, we show that the traditional wisdom that establishes that a tariff hike will always result in a real appreciation, while a terms of trade worsening will generate an equilibrium real depreciation, is incorrect.


AB This paper deals with the anatomy of devaluation in Latin America. In an effort to understand the economics surrounding the causes and consequences of exchange rate crises, eighteen devaluation episodes that took place between 1962 and 1982 are investigated in detail. The paper focuses on: (1) the relation between (inconsistent) macroeconomics policies and exchange rate crises; (2) the role of real exchange rate overvaluation in the
precipitation of balance of payment crises under pre-determined nominal exchange rates; (2) the role of exchange controls, multiple exchange rates and black markets in the period preceding devaluations; and (4) the effectiveness of nominal devaluations as a way to restore real exchange rate equilibrium. A distinction is made between stepwise devaluations and crawling per regime. It was found that historically most stepwise devaluations have had difficulty in sustaining a real devaluation over the medium term. Countries that adopted a crawling peg have generally been able to maintain a higher real exchange rate. In many cases, however, this has been achieved at the cost of substantial inflation.

Eichengreen, Barry
AB This paper provides an historical perspective on the recent behavior of the United States trade deficit. Judged by United States historical experience, the trade deficit has reached what is now unprecedented levels. That unprecedented deficit has its principal source not in changes in market structure affecting the speed with which quantities respond to prices but in the policy environment, namely the monetary-fiscal policy mix. While other industrial countries have run comparable merchandise trade deficits at various points in the past, these countries either financed their deficits out of interest earnings on prior foreign investments or through the large-scale export of services, or used the debt they incurred to finance investment in infrastructure and to expand their capacity to export. Neither of these scenarios has a counterpart in current United States experience.

Einy, Ezra
AB Using Kelley’s intersection number (and a variant of it) we define two classes of simple games, the regular and the strongly regular games. We show that the strongly regular games are those in which the set of winning coalitions and the set of losing coalitions can be strictly separated by a finitely additive probability measure. This, in particular, provides a combinatorial characterization for the class of finite weighted majority games within the simple games. We also prove that regular games have some nice properties and show that the finite regular games are exactly those simple games which are uniquely determined by their counting vector. This, in particular, generalizes a result of Chow and Lapidot.

Eldor, R.
TI Exporting Firm and Forward Markets: The Multi-Period Case. AU Zilcha, I.; Eldor, R.
TI The Demand for a Risky Asset when its Returns are Stochastically Related to Prices of Consumption Goods. AU Schwartz, A.; Pines, D.; Eldor, R.

Elmendorf, Douglas W.
TI Taxes, Budget Deficits and Consumer Spending: Some New Evidence. AU Feldstein, Martin; Elmendorf, Douglas W.

Emery, Robert F.
AB This paper examines how Taiwan, China, has used monetary policy to deal with the impact of the two oil shocks since 1973, as well as with the recent problem of a very large rise in foreign exchange holdings. In dealing with the inflationary pressures brought on by the two oil shocks, the central bank relied primarily on changes in its rediscount rate to reduce inflationary pressures. However, the changes were initially too small and too late to prevent a large rise in consumer prices in 1974 and 1980. Since 1985, the large gains in foreign exchange reserves, due to a rising trade surplus and capital inflows, have sharply expanded the money supply. The burden of containing this inflationary threat has fallen on monetary policy, and the government has not been able to offset the buildup in reserves by prepayment of external debt since the amount of outstanding debt is relatively small. In addition, use by the central bank of its rediscount policy or changes in reserve requirements has not been appropriate as domestic credit expansion has been low and not a basic cause of the large rise in liquidity. Instead, the central bank has relied almost exclusively on open market operations. It has engaged in a massive sterilization operation, selling primarily central bank certificates of deposit to neutralize the potentially inflationary impact from the large rise in the money supply. So far the central bank has been successful in holding the inflation rate to a low level, but it is not yet clear whether the present strategy will continue to be successful. Some suggestions of new basic measures for restoring a sustainable equilibrium between the external and domestic sectors are discussed.

Engel, Charles
AB Because trade liberalisation which is anticipated to be temporary creates a divergence between the effective domestic rate of interest and the world rate of interest, tariff reduction in the presence of international financial asset trade may reduce welfare for a small country. Calvo has argued that even though the government intends to liberalise trade permanently, if the private sector believes with some probability that a tariff will be imposed in the future, then free trade may not be optimal. This paper first formalises this argument and discusses the optimal policy for a government which seeks to maximise representative household welfare. The government's lack of credibility is represented by a set of beliefs the private sector holds about the type of government it faces. Next, beliefs are endogenised by allowing the private sector to update them using Bayes' rule. In one approach, the true government's objective is maximise welfare for the economy, so that it does not seek to imitate another type, in contrast with other recent models of policy credibility. With learning, the government eventually adopts free trade, even though restricted trade is optimal initially.

Epstein, Larry G.


AB This paper investigates infinite horizon intertemporal utility functions which generalise the standard additive expected utility specification. Two classes of generalisations are considered -- the first builds upon Kreps and Porteus (1978, 1979), while the second is a further generalisation which embeds the non-expected utility theory of Dekel (1986) into a multiperiod framework. Each type of generalisation has the appealing feature that it permits intertemporal substitution and risk aversion to be disentangled. Moreover, in the context of a representative agent model, each specification implies testable restrictions on the temporal behavior of consumption and asset returns.


AB This paper investigates the testable restrictions on the time-series behaviour of consumption and asset returns implied by the consumption/portfolio choice problem of an infinitely-lived, representative agent. Intertemporal preferences are characterized by utility functions that generalise conventional, time-additive, expected utility. These generalisations of expected utility, detailed in the precursor to this paper (Epstein and Zin (1987)), allow for a clear separation of observable behaviour attributable to risk aversion and to intertemporal substitution, and also provide simple nested-tests of the expected utility hypothesis. Using monthly New York Stock Exchange returns data and consumption measured with either per capita expenditures on nondurables or nondurables and services, the expected utility model is rejected. The overidentifying restrictions implied by the non-expected utility models are tested and do not, in general, lead to rejections of the theory.

Evans, Martin D. D.


AB The aim of the paper is to extend the techniques used for policy evaluation and design in continuous time rational expectations models. Following the recent literature, the optimal policy is designed in the context of a dynamic game, played between the government and the public. Using this we address the problem of time inconsistency that arises in the absence of a commitment by the government to follow the originally announced policy. Employing the concept of incentive compatibility it is shown that the government's commitment to its original policy can be determined endogenously. This allows a set of partially credible policies to be identified from which the optimal policy can be chosen. The technique is applied to a simple inflation model to illustrate how the range of policies available to the government are restricted by the requirement of incentive compatibility. It also allows the optimal policy to be examined in some detail.

Evans, Merran A.


AB This paper considers the problem of testing for heteroskedasticity in the linear regression model when one is willing to postulate only the ranking of the disturbance variances under the alternative hypothesis. A new class of tests is proposed and methods of finding the tests' critical values are discussed. An empirical power comparison with other tests that have found favor in the literature demonstrates the potential power advantage of these new
Farber, Henry S.
PD May 1987. TI The Decline of Unionization in the United States: What Can Be Learned From Recent Experience? AA Massachusetts Institute of Technology. SR Massachusetts Institute of Technology Department of Economics Working Paper: 451; Department of Economics, Massachusetts Institute of Technology, Cambridge, MA 02139. PG 36. PR No Charge. JE 831, 042. KW Unions. Wages. Working Conditions. AB The dramatic decline in unionisation over the last decade is investigated in the context of a supply/demand model of union status determination. Data from surveys conducted in 1977 and 1984 are used to decompose the decline into components due to a drop in the demand for union representation and a drop in the supply of union jobs relative to demand. It is found that there has been a substantial drop in the supply of union jobs relative to demand. It is also found that there has been a substantial drop in demand that can be accounted for by an increase in the job satisfaction of nonunion workers and a decrease in nonunion workers' beliefs that unions improve wages and working conditions. It is also found that there has been a substantial drop in the supply of union jobs relative to demand that is attributed to an increase in employer resistance to unionisation. Increased foreign and increased nonunion domestic competition (particularly in deregulated industries) are cited as the likely key underlying causes of these changes.

TI Returns to Seniority in Union and Nonunion Jobs: A New Look at the Evidence. AU Abraham, Katherine G.; Farber, Henry S.
PD August 1987. TI The Evolution of Public Sector Bargaining Laws. AA MIT. SR National Bureau of Economic Research Working Paper: 2681; National Bureau of Economic Research, 1050 Massachusetts Avenue, Cambridge, MA 02138. PR $2.00. JE 882, 881, 916, 025, 212. KW Collective Bargaining. Public Employees. Unionization. Public Policy. Markov Model. AB In 1955 only a few states had laws governing collective bargaining by public employees. By 1984 only a few states were without such laws. The emergence of these policies coincides with a dramatic increase in unionisation among public employees, and an important puzzle is the direction of causality between the laws and public employee unionisation. A key piece of the solution is understanding the evolution of the public policy in this area, and this is the focus of the analysis in this study. A Markov model of the evolution of these laws is developed based on the idea that states will change their existing policy if and only if their preferences deviate from the existing policy by more than the cost of a change in policy. The key underlying constructs are 1) the intensity of state preferences for or against public sector collective bargaining and 2) the cost of changing an existing policy or enacting a new policy. The model is implemented empirically using state level data on policy for each year from 1955 to 1984. The results suggest that state preferences for a pro-bargaining policy are positively related to 1) the COPE score (a measure of pro-union congressional voting behavior on labor issues), 2) income per capita, and 3) the size of the public sector and negatively related to southern region.

Fargeix, Andre
TI The Effect of Tariffs in Markets with Vertical Restraints. AU Perloff, Jeffrey M.; Fargeix, Andre.

Farrell, Joseph

PD January 1988. TI Cheap Talk Can Matter in Bargaining. AU Farrell, Joseph; Gibbons, Robert. AA Farrell: Department of Economics, University of California at Berkeley. Gibbons: Department of Economics, Massachusetts Institute of Technology. SR University of California at Berkeley Working Paper in Economics: 8864; IBER, 156 Barrows Hall University of California Berkeley, CA 94720. PG 27. PR $3.50. JE 026. KW Cheap Talk. Signaling. Bargaining. Negotiation. AB This paper describes an intuitive way in which cheap talk can matter in a two-stage bargaining game in which talk may be followed by serious negotiation. The intuition that all buyers would claim to have low reservation prices is incorrect in our model. Instead, the paper emphasizes that if good-faith participation is endogenously determined, then the parties can use talk to trade off bargaining position against the probability of continued negotiation. Our cheap-talk equilibrium features bargaining behavior that could not be equilibrium behavior in the absence of talk.

are made: it represents what standardization committees do. The second mechanism, by contrast, involves no explicit communication, and depends on unilateral irrevocable choices: it succeeds if one agent chooses first and the other(s) follow. This is a simple version of "market leadership." We analyze these two mechanisms in a simple model, and show that the committee is more likely to achieve coordination. Moreover, although it is slower, it outperforms the market mechanism, even when we allow for the value of speed. Third, we examine a hybrid of the first two mechanisms, in which both talk and unilateral preemptive actions are allowed. We show that, far from marring its performance, unilateral actions improve upon the committee system. This hybrid system more closely resembles the committee system the more important coordination is, relative to conflict.


AB We analyze an overlapping-generations model of duopolistic competition in the presence of consumer switching costs. Competition for established buyers is continually intermingled with competition for new, uncommitted buyers. In equilibrium, the firm with attached customers typically specializes in serving them and concedes the new buyers to its rival. This pattern of repeated entry persists even when there are economies of scale or network externalities. Switching costs thus can cause inefficiency in a surprising way: far from forming an entry barrier, they encourage entry to serve new customers even when such entry is inefficient.

**Feenstra, Robert C.**


AB In this paper we consider a home government with political pressure to restrict trade, at the expense of foreigners. The foreign country is compensated with an income transfer, which can be thought of as a portion of the tariff revenues or quota rents. In this setting the two countries should negotiate over the level of tariff and transfer of rents, depending on the level of political pressure at home. However, if this pressure cannot be directly observed abroad, then the home country may have an incentive to claim arbitrarily high political need and seek corresponding high trade barriers. We resolve this problem by determining incentive compatible trade policies, in which the home government has no incentive to overstate (or understate) the political pressure for protection.


AB This paper examines the effect of tariffs and exchange rates on U.S. prices of Japanese cars, trucks and motorcycles. In particular, we test whether the long run pass-through of tariffs and exchange rates are identical: the symmetry hypothesis. We find that this hypothesis is easily accepted in our sample. We also find that the pass-through relation varies across products, ranging from about 0.6 for trucks to unity for motorcycles. These coefficients have very different implications for trade policy. We explain the results based on demand, cost and institutional conditions in each industry. We also find weak evidence that the pass-through of exchange rates has fallen in more recent years.

**Feenstra, Robert C. Feldstein, Martin**


AB Because of the restrictive assumptions required to establish the theory of Ricardian equivalence, its relevance in practice is essentially an empirical question. The strongest direct evidence in favor of Ricardian equivalence is Roger Kormendi's (1983) article in the American Economic Review. That paper appeared to provide strong empirical support for Ricardian equivalence by showing that increases in government spending on goods and services depress consumer spending while changes in tax receipts have no effect on consumer spending. The present study shows that Kormendi's results are a misleading implication of the experience during World War II when shortages, rationing and patriotic appeals to self-restraint caused an abnormally high rate of saving at the same time that the government deficit-financed a uniquely massive increase in defense spending. When those years are excluded from the sample, Kormendi's results are reversed.

This paper presents a method of studying the distributional consequences of corporate tax changes by imputing to individual tax returns the net effect of changes in effective corporate tax rates. Particular attention is given to the difference between nominal and real capital income, to the problem of corporate pension funds, and to the automatic effect of corporate tax changes on dividends and retained earnings.

Fershtman, Chaim

PD January 1988. TI Cooperation through Delegation. AU Fershtman, Chaim; Judd, Kenneth L.; Kalai, Ehud. AA Fershtman: Department of Economics, Tel-Aviv University. Kalai and Judd: Department of Managerial Economics and Decision Sciences J.L. Kellogg Graduate School of Management, Northwestern University. SR Tel-Aviv Foerder Institute for Economic Research Working Paper: 5-88; Department of Economics, Tel-Aviv University, Ramat Aviv 69978, Tel-Aviv, ISRAEL. PG 18. PR No Charge. JE 026, 611. KW Delegation. Cooperation. Folk Theorem. Noncooperative Game. AB Most economics and political games are played by agents of the real players. This paper analyzes the outcomes of general noncooperative games in which the players can strategically use agents to play on their behalf. It is shown that when players in a noncooperative game delegate strategy choices to their agents every Pareto optimal outcome of the game becomes a Nash equilibrium of the delegation game. A folk theorem using delegation game is presented. The result casts serious doubt about the properness of many models applying game theory to the analysis of economic activity.

PD January 1988. TI The Strategic Aspects of Privatisation of Oligopolistic Firms. AA Department of Economics, Tel-Aviv University. SR Tel-Aviv Foerder Institute for Economic Research Working Paper: 3-88; Department of Economics, Tel-Aviv University, Ramat Aviv 69978, Tel-Aviv, ISRAEL. PG 27. PR No Charge. JE 022, 611, 614, 612. KW Privatization. Public Enterprise. Oligopoly. Market Structure. Natural Monopoly. AB One of the common justifications for privatization policy is the assertion that private firms are more efficient and thus potentially more profitable. Our main claim in this paper is that the analysis of privatization policy cannot be complete without a specific attention to the market structure in which the firm operates. We deviate from the standard assumption that a firm is either private or nationalized and discuss the possibility of partial privatization. We examine a duopolistic market and demonstrate that a partly nationalized firm might realize higher profits than its private, profit maximizing, competitor. Moreover this result may hold even if we assume that there is some degree of cost inefficiency associated with nationalization. The degree of nationalisation affects also the interaction between an incumbent firm and a potential entrant. Using Dixit (1980) framework we discuss the implications of privatization on the attractiveness of entry, the possibility to deter entry and the incumbent position as a natural monopoly. We show that it is possible that a firm is not a natural monopoly while being private but altering its ownership structure so it becomes partly nationalised can transform the firm to a natural monopoly.

PD January 1988. TI Turnpike Properties in a Finite Horizon Differential Game; Dynamic Duopoly With Sticky Prices. AU Fershtman, Chaim; Kamien, Morton I. AA Fershtman: Department of Economics, Tel-Aviv University. Kamien: Department of Managerial Economics and Decision Sciences, J.L. Kellogg Graduate School of Management, North Western University. SR Tel-Aviv Foerder Institute for Economic Research Working Paper: 4-88; Department of Economics, Tel-Aviv University, Ramat Aviv 69978, Tel-Aviv, ISRAEL. PG 22. PR No Charge. JE 026, 022, 611. KW Feedback Nash Equilibrium. Differential Games. Dynamic Duopoly. Turnpike Properties. AB The main purpose of this paper is a complete analysis of the feedback Nash equilibrium of a finite horizon linear quadratic differential game and the relationship between the finite horizon equilibrium and the infinite horizon equilibrium. We use a previous model (Fershtman & Kamien (1987) in which we studied an infinite horizon model of dynamic duopolistic competition under the assumption of price stickiness to investigate the relationship between the finite and infinite horizon game.

Figlewski, Stephen
PD June 1987. TI Options Arbitrage in Imperfect Markets. AA New York University. SR New York University Salomon Brothers Center Working Paper: 430; Salomon Brothers Center, Graduate School of Business Administration, New York University, 100 Trinaty Place, New York, NY 10006. PG 31. PR $3.00. JE 511, 513, 026. KW Option Valuation Model. Options Markets. Stock Index Options. Uncertainty. Volatility. Risk. Arbitrage Mechanism. Securities Trading. AB Option valuation models are generally derived in a frictionless market setting using an arbitrage argument. Actual options markets are subject to many imperfections that are sufficiently complex that a general theoretical treatment is infeasible. This paper adopts a simulation approach to examine some of the more important imperfections of a market similar to that for exchange traded stock index options, uncertainty about the volatility of the underlying asset: transactions costs, indivisibilities, and the impossibility of rebalancing a
hedge portfolio continuously. The clear result of our analysis is that the arbitrage mechanism that is the basis for theoretical pricing models in a frictionless market is exposed to considerable risk and large transactions costs in our actual, imperfect, markets. The risk and expected cost of hedging an option with the underlying asset and carrying the position until option expiration is so great compared to typical bid-ask spreads in the market as to be not a viable strategy even for the lowest cost transactor. This has important implications for marketmaking and price determination in options markets.

Fischer, Stanley
AB Since August 1982 the international debt crisis has dominated economic policymaking in the developing countries, economic relations between the debtor and creditor countries, the attention of the multilateral institutions in their dealings with the debtor nations, and private sector decisions on lending to the developing countries. Three classes of solutions are described and evaluated. Least radical are proposals for procedural reform and changes in the nature of the claims on the existing debt. The second type of solution is the creation of a facility, or new institution to deal with the overhang of existing debt. Finally, there are proposals for debt relief, either in direct negotiation between creditors and debtors and/or in conjunction with the creation of a facility.

Fisher, Anthony C.
AB This paper suggests a likely course of oil prices over the next several years on the basis of theoretical models of the world oil market calibrated to pre-1973 levels of prices, production, and reserves. The current (1986) competitive environment, with price in the $10-$16 per barrel range and increasing very gradually, should prevail until the early 1990s. At that time excess supply and excess capacity in the industry will all but disappear, making a jump to the Organization of Petroleum Exporting Countries cartel's joint wealth-maximizing price of about $25-$30 per barrel likely.

AB This paper explores the uses of economic theory in understanding what many non-economists regard as the major environmental problem of our time -- the coming mass extinction of species. In the present paper, I wish to offer a couple of models, drawing on more recent work by myself and others, to describe key aspects of the problem of species extinction: habitat loss and overexploitation.

Fisher, Franklin M.
AB In the Edgeworth non-tatonnement process, trade occurs if there exists some coalition of agents able to make a Pareto-improving trade among themselves at current prices. It is known that the size of such coalitions is bounded by the number of commodities and that, provided all agents always have strictly positive endowments, bilateral trade suffices. These results are generalised: Let there be h agents, k of whom have strictly positive endowments. Let there be m commodities, n of which are held by all agents. Then the Edgeworth-process requires coalitions with at most t* = Min [2, Max (h - k, m - n)] members. This is a least upper bound.

Fleising, A.
TI University Policies under Varying Market Conditions: The Training of Electrical Engineers. AU Eckstein, Z.; Weiss, Y.; Fleising, A.

Forges, Françoise
AB To gather information from n informed agents, a principal can rely on a mediator. Does there exist a direct communication scheme yielding the same equilibrium payoffs? Yes, as soon as extraneous signals ("sunspots") can be observed before the beginning of the game.

Forsythe, Robert
The paper describes an experiment involving a set of pie-splitting games between two players. The pie is a sum of money, $P_i$, which takes the values $P_i \text{sub} g$ (good) with probability $p$ and $P_i \text{sub} b$ (bad) with probability $(1-p)$. One bargainer knows the realised value of $P_i$ while the other is uninformed. The bargainers are in separate rooms, and negotiate by sending nonbinding handwritten messages back and forth, and also by making binding proposals as to how much money the uninformed player is to receive. If agreement is not reached within 10 minutes, then neither bargainer gets anything. If the uninformed bargainer had the right to make non-negotiable demands, then he would demand $P_i \text{sub} g$ ("play tough") if $P_i \text{sub} g > P_i \text{sub} b$, and otherwise demand $P_i \text{sub} b$ ("play soft"). We refer to this as the strike condition: if it holds the bargainers will fail to agree whenever the bad pie is drawn. In our experiment, however, no one had the right to make non-negotiable demands. The main prediction is that strikes will occur when the strike condition is on, and then only when the bad pie is drawn. Beyond this, Myerson's Neutral Bargaining Solution is used to predict the value of the game for the uninformed and informed players.

Frank, Andras

AB If we are interested in various properties of graphs it is often useful to dismantle the graph into connected components and then investigate those components separately. For example, to decide whether a graph is k-colorable it suffices to deal with the connected components. A similar idea works for higher connectivity as well. In this chapter we try to provide a rather comprehensive overview of results belonging to this area. Certain (mostly easier) parts are discussed in greater details in order to give some hints on the general techniques used. Other parts are more difficult so we confine ourselves to give a general framework filled with various results but no proofs. Certain (mostly easier) parts are discussed in greater details in order to give some hints on the general techniques used. Other parts are more difficult so we confine ourselves to give a general framework filled with various results but no proofs. In some cases, however, when it did not need too much space, proofs of some deep theorems (e.g. Tutte's wheel theorem, Nash-Williams theorem on covering trees) have been included.

Frank, Richard

AB We employ a unique data set from a community based survey to assess the effect of mental distress on earnings. The main advantage of the data is that detailed measurements of mental health status were made on all subjects in the study. This means that our population-based measure of mental distress does not rely on a patient having had contact with the health care system and obtaining a diagnosis from a provider. The use of diagnosis-based measures may introduce measurement-error bias into the estimates. Our results show that the presence of mental distress reduces earnings by approximately 21 per cent to 33 per cent. To assess the magnitude of any measurement-error bias we present a "estimate" of models using measures of mental health both on a population-wide basis and on a diagnosis basis. The estimated impact of mental illness on earning is only 9 per cent lower using the diagnosis-based measure. The conclusion drawn from this is that little bias is introduced by using the diagnosis-based measure.

Frankel, J.

AB We consider an application of bootstrap ideas to kernel estimates of spectral densities of stationary time series. We prove that the bootstrap principle holds in the same sense as in parametric and nonparametric estimation of regression curves. The general approach is illustrated with specific applications like a bootstrap method for choosing the bandwidth of a kernel estimate. In particular, we show that this method provides a consistent and asymptotically optimal bandwidth.

Frankel, Jeffrey A.

AB We relax the assumption of the literature on international coordination that policy-makers know the true model. Two countries will still be able to agree on a cooperative policy package that each believes will improve the objective function relative to the Nash non-cooperative solution. However, the bargaining solution may move the target variables in the wrong direction. These points are illustrated with monetary and fiscal multipliers taken from simulations of ten leading econometric models. Out of 1000 possible combinations of models that could represent United States beliefs, non-United States beliefs and the true model, monetary coordination improves United States welfare in only 548 cases.
**ABSTRACTS**


**AB The optimal-diversification model of investors' portfolio behavior can give a linear relationship between the exchange risk premium and the conditional exchange rate variance. This note surveys recent empirical work that allows for the conditional variance itself, and therefore the risk premium, to vary over time. In particular, it examines the implications of recent empirical estimates for earlier arguments, based on the assumption that the conditional variance was constant over time, that the exchange risk premium had to be small in magnitude and variability.**

**Freeman, Richard B.**


**Froot, Kenneth A.**


**AB Survey data on interest rate expectations are used to separate the forward interest rate into an expected future rate and a term premium. These components are used to test separately two competing alternative hypotheses in tests of the term structure: that the expectations hypothesis does not hold, and that expected future long rates are insufficient to predict future interest rate changes, expected future long rates do not hold, and that expected future long rates are insufficient to predict future interest rate changes. While the spread consistently fails to predict future interest rate changes, we find that the nature of this failure is different for short versus long maturities. For short maturities, expected future rates are rational forecasts. The poor predictions of the spread can therefore be attributed to variation in term premis. For longer-term bonds, however, we are unable to reject the expectations theory, in that a steeper yield curve reflects a one-for-one increase in expected future long rates. Here the perverse predictions of the spread reflect investors' failure to raise sufficiently their expectations of future long rates when the short rate rises. We confirm earlier findings that bond rates underreact to short rate changes, but now this result cannot be attributed to the term premium.**


**AB Simple regression tests that have power against the alternatives that asset prices and expected future asset returns are excessively volatile are developed and performed for the foreign exchange and stock markets. These tests have a number of advantages over alternative, variance bounds techniques. We find evidence that both exchange rates and stock prices are excessively volatile and that expected returns on foreign exchange and stocks move too much. We also investigate whether these findings can be attributed to time-varying risk premia, but in our tests the data provide little support for such an alternative hypothesis.**


**AB This paper investigates the effects of imperfectly credible trade liberalization programs on welfare and the allocation of real resources. We present a rational expectations model in which a government with limited access to international financial markets may be forced to abort a liberalisation program if hard-currency reserves are depleted too quickly. The liberalization's lack of perfect credibility acts as a distortion which becomes (rationally) intensified under the typical first-best policy of a direct move to free trade. A gradual lowering of trade barriers turns out to be welfare-superior to an immediate liberalisation, and to improve the chance that the program will ultimately succeed. We then derive the optimal speed of liberalisation, the intertemporal allocation of resources, and the liberalization program's credibility.**

**Fudenberg, Drew**


**AB In this paper we are interested in the lower hemi-continuity of the Nash equilibrium correspondence with respect to the number of players. Specifically, given an equilibrium in a game with a continuum of players, and a finite player game that approximates the continuum game, is there an equilibrium of the finite player game that is "close" to the equilibrium of the continuum game?**


AB Non-cooperative game theory is a way of modelling and analysing situations in which each player's optimal decisions depend on his beliefs or expectations about the play of his opponents. The distinguishing aspect of the theory is its insistence that players should not hold arbitrary beliefs about the play of their opponents. Instead, each player should try to predict his opponents' play, using his knowledge of the rules of the game and the assumption that his opponents are themselves rational, and are thus trying to make their own predictions and to maximize their own payoffs. Game-theoretic methodology has caused deep and wide-reaching changes in the way that practitioners think about key issues in oligopoly theory, much as the idea of rational expectations has revolutionized the study of macroeconomics. This essay tries to provide an overview of those aspects of the theory which are most commonly used by industrial organization economists, and to sketch a few of the most important or illuminating applications. We have omitted many interesting game-theoretic topics which have not yet been widely applied.


AB The philosophy of equilibrium refinements is that the analyst, if he knows things about the structure of the game, can reject some Nash equilibria as unreasonable. The word "know" in the preceding sentence deserves special emphasis. If in a fixed game the analyst can reject a particular equilibrium outcome, but he cannot do so for games arbitrarily "close by", then he may have second thoughts about rejecting the outcome. We consider several notions of distance between games, and we characterize their implications for the robustness of equilibrium refinements.

Fullerton, Don

PD August 1987. TI The Marginal Excess Burden of Different Capital Tax Instruments. AU Fullerton, Don; Henderson, Yolanda K. AA Fullerton: University of Virginia. Henderson: Federal Reserve Bank of Boston. SR National Bureau of Economic Research Working Paper: 2553; National Bureau of Economic Research, 1050 Massachusetts Avenue, Cambridge, MA 02138. PG $2.00. JE 523. KW Tax Burden. Welfare Loss. Capital Taxes. Income Tax. Taxation. General Equilibrium Model. Investment Tax Credit. Distortions. AB Marginal excess burden, defined as the change in deadweight loss for an additional dollar of tax revenue, has been measured for labor taxes, output taxes, and capital taxes generally. This paper points out that there is no well-defined way to raise capital taxes in general, because the taxation of income from capital depends on many different policy instruments including the statutory corporate income tax rate, the investment tax credit rate, depreciation lifetimes, declining balance rates for depreciation allowances, and personal tax rates on noncorporate income, interest receipts, dividends, and capital gains. Marginal excess burden is measured for each of these different capital tax instruments, using a general equilibrium model that encompasses distortions in the allocation of real resources over time, among industries, between the corporate and noncorporate sectors, and among diverse types of equipment, structures, inventories, and land.


AB Many studies measure capital stocks and effective tax rates for different industries, but they consider only tangible assets such as equipment, structures, inventories, and land. However, firms also own intangible assets such as trademarks, copyrights, patents, a good reputation, or general production expertise. This paper provides alternative measures of the intangible capital stock, and it investigates implications for distortions caused by taxes. The existence of intangible capital markedly alters welfare cost calculations. Investments in advertising and R&D are expensed, so the effective rate of tax on these assets is less than that on equipment under prior law. With large differences between these assets and other tangible assets, we find that the welfare cost measure under prior law increases to $13 billion per year. Repeal of the investment credit taxes equipment more like other tangible assets but less like intangible assets. The welfare cost still falls, to about $7 billion per year, but it is no longer "virtually eliminated." With additional sources of intangible capital, credit repeal could actually increase welfare costs. Finally, however, the Tax Reform Act of 1986 not only repeals the investment tax credit but reduces rates as well. Efficiency always increases in this model because the taxation of tangible assets is reduced toward that of intangible assets.

Geanakoplos, J.


AB This paper studies a general equilibrium model of a stock market economy in which the structure of markets is incomplete. We show that generically (in endowments)
equilibrium allocations are constrained inefficient. Thus under a competitive price taking system decentralised decision-making does not lead to an efficient use of markets.

Gertler, Paul
TI The Effect of Mental Distress on Income: Results from a Community Survey. AU Frank, Richard; Gertler, Paul.

Gertner, Robert
AB This paper analyses an informed firm's choice of financial structure using what we call a two-audience signaling model: the choice of a financing contract is observed not only by the capital market, but also by a second interested (but uninformed) party. This second party might be a competing firm or a labor union. A key feature of the model is that the informed firm's gross profit is endogenous, because the second party's action depends on the transaction it observes between the informed firm and the capital market. The main result is that the reasonable capital-market equilibria (i.e., those that satisfy a refinement) maximize the ex-ante expectation of the informed firm's endogenous gross product-market profits. In this sense, the character of capital-market equilibrium is determined by the structure of the product market. An immediate corollary is that (generically) either all the reasonable equilibria are separating or all the reasonable equilibria are pooling. Indeed, the latter is often the case. This is in distinct contrast to earlier work on the information content of financial structure and to more recent work on refinement in signaling games, both of which focus on separating equilibria.

Ghali, Khalifa
TI Self-Selection in the Residential Electricity Time-of-Use Pricing Experiments. AU Aigner, Dennis J.; Ghali, Khalifa.

Gibbons, Robert
TI Simultaneous Signaling to the Capital and Product Markets. AU Gertner, Robert; Gibbons, Robert; Scharfstein, David. TI Cheap Talk Can Matter in Bargaining. AU Farrell, Joseph; Gibbons, Robert.

Gilbert, Christopher
PD September 1987. TI The Management of Developing Country Commodity Risks: A New Role for Public Policy. AU Gilbert, Christopher; Powell, Andrew. AA Institute of Economics and Statistics, University of Oxford. SR Oxford Applied Economics Discussion Paper: 34; Institute of Economics and Statistics, St. Cross Building, Manor Road, Oxford OX1 3UL, ENGLAND. PG 47. PR No Charge. JE 121, 815, 431, 441. KW International Commodity Agreements. Debt. Futures. Options. Puts. Calls. Risk Management. LDCs. Commodities. Commodity Markets. AB The management of high commodity risks remains a major problem for LDCs. Intervention in primary goods markets through International Commodity Agreements has met with limited successes and notable failures. During the same period risk management in financial markets has undergone significant changes and there are important lessons for commodity risk management from new products created. Commodity risks and financial risks are intimately related in many LDCs; the risk in servicing debt, for example, is related to commodity export earnings. The usual risk-sharing, moral-hazard trade-off applies to the use of contingent payment structures. Commodity-linked bonds might be used to "manage" the trade-off but there are strong arguments that only a limited set of long term contracts will be supported by the private markets due to serious performance risks. Public policy might then be viewed as the augmentation of private markets by underwriting some part of the default risk.

Gilboa, Itzhak
TI Value for Two-Stage Games: Another View of the Shapley Axioms. AU Beja, Avraham; Gilboa, Itzhak.

Ginsburgh, Victor
PD December 1987. TI Price Discrimination and Product Line Rivalry. AU Ginsburgh, Victor; MacLeod, Bentley; Weber, Shlomo. AA Ginsburgh: Universite Libre de Bruxelles, CORE. MacLeod: Queen's University, Kingston, Canada. Weber: York University and the University of Haifa. SR Queen's Institute for Economic Research Discussion Paper: 702; Department of Economics, Queen's University, Kingston, Ontario, CANADA K7L 3N6. PG 46. PR Canada & U.S. $3.00; $3.50 foreign. JE 611, 022, 633. KW Price Discrimination. Oligopoly. Automobile. Differentiated Product. AB We introduce a model of oligopolistic price setting in which products are characterized by both style and
quality. Producers are identified by a style, unique to
to their product line and a range of qualities, and are to price
discriminate among consumers using quality. We study
the properties of the equilibrium for this model and show,
in contrast to Mussa and Rosen's work on the
discriminating monopolist, that firms do not necessarily
extract the most surplus from consumers of low quality
products. The amount of surplus extracted as a function
of quality will depend on the underlying demand
parameters. The model is then used as the basis for
estimating the pricing strategies of firms in the European
automobile market. We find that the level of price
discrimination varies greatly from country to country.
More surprisingly, we find that the quality parameter that
firms use to discriminate among consumers appears to be
engine capacity. This may explain why engine capacity
seems to be the only technical characteristic of the car that
is often prominently displayed on the vehicle.

PD February 1988. TI Price Discrimination and
Product Line Rivalry. AU Ginsburgh, Victor; MacLeod,
Bentley; Weber, Schlomo. AA Ginsburgh: Universite
Libre de Bruxelles. MacLeod: Queens University,
Kingston. Weber: University of Haifa. SR Universitat
Bonn Sonderforschungsbereich 303 - Discussion Paper:
B-92; Sonderforschungsbereich 303 an der Universitat Bonn,
Adenauerallee 24-42, D-5300 Bonn 1, DEUTSCHLAND.
PG 58, PR No Charge. JE 611, 022, 655, 212.
KW Oligopoly. Price Setting. Automobile. Differentiated
Product. Discrimination.

AB We introduce a model of oligopolistic price setting in
which products are characterized by both style and
quality. Producers are identified by a style, unique to
their product line and a range of qualities, and are to price
discriminate among consumers using quality. We study
the properties of the equilibrium for this model and show,
in contrast to Mussa and Rosen's work on the
discriminating monopolist, that firms do not necessarily
extract the most surplus from consumers of low quality
products. The amount of surplus extracted as a function
of quality will depend on the underlying demand
parameters. The model is then used as the basis for
estimating the pricing strategies of firms in the European
automobile market. We find that the level of price
discrimination varies greatly from country to country.
More surprisingly, we find that the quality parameter that
firms use to discriminate among consumers appears to be
engine capacity. This may explain why engine capacity
seems to be the only technical characteristic of the car that
is often prominently displayed on the vehicle.

Glazer, Jacob

TI Sharing Productive Knowledge in Internally
Financed R&D Contests. AU Bhattacharya, Sudipto;
Glazer, Jacob; Sappington, David E. M.

TI Motivating Exchange of Knowledge in R&D
Ventures: First-Best Implementation. AU Bhattacharya,
Sudipto; Glazer, Jacob; Sappington, David.

Glyn, Andrew J.

PD September 1987. TI A Case for Exchange
Controls. AA Corpus Christi College, Oxford.

Institute of Economics and Statistics, St. Cross Building,
Manor Road, Oxford OX1 3UL, ENGLAND. PG 47,
PR No Charge. JE 431, 432, 441, 311, 321.
KW United Kingdom Economy, International Finance.
Flight. Monetary Policy.

AB The trend towards the increased international
financial involvement of the United Kingdom economy is
analysed and it is argued that the potential for capital
flight makes it impossible for a government to implement
an expansionary program aimed at full employment.
Various proposals for limiting vulnerability to capital
flight are analysed and it is concluded that only a
comprehensive system of exchange controls could be
adequate to the task. One outline for such a system is
proposed, political and technical difficulties are considered
and historical and international comparisons outlined.

Gofin, J. L.

PD September 1987. TI Affine Methods in
Nondifferentiable Optimisation. AA McGill University.
SR Universite Catholique de Louvain CORE Discussion
Paper: 8744; Universite Catholique de Louvain Voie du
Roman Pays, 34, B-1348 Louvain-la-Nueve BELGIUM.
PG 24, PR No Charge. JE 213, 022. KW Convex
Algorithm. Ellipsoid Method.

AB The problem studied is that of minimising a general
(nondifferentiable) convex function. We wish to emphasize
the difference in convergence proofs between the case of a
convex polyhedral function given explicitly by a finite
number of linear pieces to that of a convex function which

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is generated by successive calls to an oracle (subroutine) which returns cutting planes, that is the function value and one arbitrary subgradient. The methods used are either exterior ellipsoid methods (the ellipsoid method) or interior ellipsoid methods (affine variants of Karmarkar's algorithm). Computational results using a "dual affine method", implemented within the space of the graph of the function, are given, for the case of general -- nondifferentiable -- convex functions defined by generated cutting planes.

Goldfeld, Stephen M.

AB Motivated by the notion of the soft budget constraint, we develop two models of an enterprise that can secure bailouts from the state when its operating profit is negative. The models allow for uncertainty both in production and in the extent to which the enterprise can obtain subsidies. We derive the optimal factor inputs and show, both via theorems and illustrative calculations, how the availability of bailouts increases the demand for factor inputs. The dependence of this increase on the features of the bailout process is also characterized.

Gollier, Christian

AB The labour market has failed to spread risk among different generations. Unlucky generations entering the labour market during a recession bear almost all risks, whereas older workers are protected by implicit contracts offering a downward rigid wage. Using three two-period models with overlapping generations of workers, we analyze the conflict of interest between insiders with a contract and outsiders (unemployed and the young cohort entering the labour market). The wage discrimination between generations will depend upon the incentive of insiders to raise the hiring wage. An intermediary wage discrimination is shown to be efficient in order to promote employment for outsiders, although limiting the cost of layoff for insiders.

Goodstein, Eban
TI Committee Voting Under Alternative Procedures and Preferences: An Experimental Analysis. AU Salant, Stephen; Goodstein, Eban.

Gordon, James P. F.
TI Unwillingness to Pay: Tax Evasion and Public Good Provision. AU Cowell, Frank A.; Gordon, James P. F.

Gordon, Roger H.

AB This paper shows, using a standard CAPM model of security prices in a world market, that even small countries can affect the price of domestically issued risky securities, while large countries can affect the prices of all securities. As a result, countries have the incentive to set tax rates such that in equilibrium investors tend to specialize in domestic securities, and net capital flows between countries are restricted. Each country does this to increase the utility of domestic residents, taking as given the tax policies of other governments, but the net outcome is a reduction in world efficiency and likely a reduction in the utility of all investors.


AB In this paper we examine government debt and tax-transfer policies that can improve the allocation of risk between generations. Markets cannot allocate risk efficiently between two generations whenever the two generations are not both alive prior to the occurrence of a stochastic event. This implies that government policies transferring risk between generations have the potential to create first-order welfare improvements. Our model provides a non-Keynesian justification for debt-finance of wars and recessions, as well as an added rationale for Social Security type tax-transfer schemes which aid unlucky generations, e.g., the Depression generation, at the expense of luckier generations.

Gourieroux, C.

AB A general framework for asymptotic tests is proposed. This framework contains as particular cases tests based on various estimation techniques: maximum likelihood methods, pseudo-maximum likelihood (P.M.L.)
methods and quasi-generalized P.M.L. methods, m-
estimation methods, moments or generalized moments
method, asymptotic least squares. Moreover the null
estimation methods, moments or generalized moments
method, asymptotic least squares. Moreover the null
hypothesis has a general "mixed" form, including the usual
implicit and explicit form.

PD October 1987. TI Contraintes bilineaires:
estimation et test. AU Gourieroux, C.; Monfort, A.;
Renault, E. AA Gourieroux: CEPREMAP. Monfort:
INSEE. Renault: Paris IX et E.N.S. SR Unite de
Recherche Document de Travail ENSAE/INSEE: 8712;
INSEE, Unite de Recherche, 18 Bd. Adolphe Pinard, 75675
Paris cedex 14, FRANCE. PG 48. PR No Charge.
JE 211. KW Asymptotic Tests. Asymptotic Least

AB In this paper we propose a Wald type test procedure
for the case where the null hypothesis is in a mixed form
and bilinear with respect to the parameter of interest and
an auxiliary parameter. This procedure is very simple
since it only requires O.L.S. and G.L.S. methods.
Moreover, it provides estimators of the parameters under
the null hypothesis. It is also shown that these theoretical
results apply to many situations: common roots,
distributed lags, instrumental variables, overidentification,
rational expectation, separability and homotheticity of
translog functions.

PD October 1987. TI Testing Price Exogeneity in the
Canonical Disequilibrium Model. AU Gourieroux, C.;
Laroque, G. AA Gourieroux: CEPREMAP. Laroave:
INSEE. SR Unite de Recherche Document de Travail
ENSAE/INSEE: 8713; INSEE, Unite de Recherche, 18 Bd.
Adolphe Pinard, 75675 Paris cedex 14, FRANCE.
PG 26. PR No Charge. JE 211. KW Asymptotic
Tests. Disequilibrium Model.

AB The paper describes some tests of the exogeneity of
prices in the canonical disequilibrium model supplemented
with a price adjustment equation. We also develop a
technique which allows to estimate consistently the
demand and supply equations, using the standard us
disequilibrium software, when the price variable is not
exogenous.

Greenwood, J.

PD October 1987. TI Investment, Capacity
Utilisation and the Real Business Cycle. AU Greenwood,
J.; Hercowits, Z.; Huffman, Gregory W. AA Greenwood:
University of Western Ontario. Huffman: University of
Western Ontario. Hercowits: Tel Aviv University.
SR Tel Aviv Foerder Institute for Economic Research
Working Paper: 26-87; Department of Economics, Tel
Aviv University, Ramat Aviv 69978, Tel Aviv, ISRAEL.
PG 39. PR No Charge. JE 112, 522, 023.
KW Capacity Utilisation. Real Business Cycle. Shocks to
Marginal Efficiency of Investment.

AB This paper adopts Keynes' view that shocks to the
marginal efficiency of investment are important for
business fluctuations, but incorporates it in a neoclassical
framework with endogenous capacity utilisation. Increases
in the efficiency of newly produced investment goods
stimulate the formation of "new" capital and the more
intensive utilization of "old" capital. Theoretical and
quantitative analysis suggests that the shocks and
transmission mechanism studied here may be important
elements of business cycles.

Gregory, Allan W.

PD September 1987. TI A Nonparametric Test for
Autoregressive Conditional Heteroskedasticity (ARCH): A
Markov Chain Approach. AA Department of Economics,
University of Western Ontario. SR University of
Western Ontario Department of Economics Research
Report: #8713; Department of Economics, Social Sciences
Center, University of Western Ontario, London, Ontario,
CANADA N6A 5C2. PG 25. PR $5.00 Canada; $7.00
Elsewhere. JE 211. KW Conditional Heteroskedasticity.

AB In this paper we propose a nonparametric test for
autoregressive conditional heteroskedasticity (ARCH)
based upon finite state Markov chains. A simple Monte
Carlo experiment suggests that in finite samples it
performs comparably to the LM test under conditional
normality and is superior for the t-, lognormal, and
exponential distributions. As an illustration, we apply
both tests to Canadian/United States forward foreign
exchange data.

PD December 1987. TI Calibration as Estimation.
AU Gregory, Allan W.; Smith, Gregor W. AA Gregory:
University of Western Ontario. Smith: Queen's University.
SR Queen's Institute for Economic Research Discussion
Paper: 700; Department of Economics, Queen's University, Kingston, Ontario,
CANADA K7L 3N6. PG 46. PR $3.00 Canada and
U.S.; $5.50 Foreign. JE 211. KW Calibration. Method
of Moments. Monte Carlo.

AB One aspect of calibration in macroeconomics is the
notion that the free parameters of models should be chosen
by matching certain moments of the simulated models
with those of actual data. We formally examine this
notion by treating the process of calibration as an
econometric estimator. A numerical version of the
Mehra-Prescott (1988) economy is the setting for an evaluation of
calibration estimators via Monte Carlo methods. While
these estimators sometimes may have reasonable finite-
sample properties they are not robust to mistakes in
setting non-free parameters. In contrast, generalised
method-of-moments (GMM) estimators have satisfactory
finite-sample characteristics, quick convergence, and
informational requirements less stringent than those of
consistent calibration estimators. In dynamic equilibrium
models in which GMM is infeasible we offer some
suggestions for improving estimates based on calibration
methodology.

Grossman, Herschel

PD November 1987. TI Lending to an Insecure
Sovereign. AA Brown University. SR National
National Bureau of Economic Research, 1050
Massachusetts Avenue, Cambridge, MA 02138.
PG 1. PR $2.00. JE 449, 322, 114, 921. KW Sovereign

AB This paper analyzes a reputational equilibrium for
sovereign debt in a model in which the sovereign borrows
to finance spending for defense against threats to its
survival in power. In this model, the amount of sovereign
debt and defense spending, the resulting survival
probability, and the sovereign's implied discount rate for future consumption are determined simultaneously. The optimal amount of debt and defense spending equates the marginal cost of defense spending in reducing the level of consumption to the marginal benefit of defense spending in increasing the probability of surviving to enjoy future consumption. In the reputational equilibrium, however, the amount of debt and the associated discount rate must be small enough that the short-run gains from debt repudiation are not larger than the long-run costs from the loss of a trustworthy reputation.

**Grossman, Michael**

TI A Cost-Effectiveness Analysis of Strategies to Reduce Infant Mortality. AU Corman, Hope; Joyce, Theodore; Grossman, Michael.

**Grossman, Sanford**


AB We analyze a model of optimal consumption and portfolio selection in which consumption services are generated by holding a durable good. The durable good is illiquid in that a transaction cost must be paid when the good is sold. We characterize the optimal behavior of the consumer. We show the large impact of transaction costs on the consumers behavior through numerical simulations, with plausible parameters evaluated from United States data.


AB We analyze a model of optimal consumption and portfolio selection in which consumption services are generated by holding a durable good. The durable good is illiquid in that a transaction cost must be paid when the good is sold. It is shown that optimal consumption is not a smooth function of wealth; it is optimal for the consumer to wait until a large change in wealth occurs before adjusting his consumption. As a consequence, the consumption based capital asset pricing model fails to hold. Nevertheless, it is shown that the standard, one factor, market portfolio based capital asset pricing model does hold in this environment. It is shown that the optimal durable level is characterized by three numbers (not random variables), say x, y, and z (where x < y < z). The consumer views the ratio of consumption to wealth (c/W) as his state variable. If this ratio is between x and s, then he does not sell the durable. If c/W is less than x or greater than s, then he sells his durable and buys a new durable of size S so that S/W = y. Thus y is his "target" level of c/W. If the stock market moves up enough so that c/W falls below x, then he sells his small durable to buy a larger durable. However, there will be many changes in the value of his wealth for which c/W stays between x and s, and thus consumption does not change. Numerical simulations show that small transactions costs can make consumption changes occur very infrequently. Further, the effect of transactions costs on the demand for risky assets is substantial.


AB Recent advances in financial theory have created an understanding of the environments in which a real security can be synthesized by a dynamic trading strategy in a risk free asset and other securities. We contend that there is a crucial distinction between a synthetic security and a real security. Portfolio insurance provides a good example of the difference between a synthetic security and a real security. One form of portfolio insurance uses a trading strategy in risk free securities ("cash") and index futures to synthesize a European put on the underlying portfolio. In the absence of a real traded put option (of the appropriate striking price and maturity), there will be less information about the future price volatility associated with current dynamic hedging strategies. There will thus be less information transmitted to those people who could make capital available to liquidity providers. It will therefore be more difficult for the market to absorb the trades implied by the dynamic hedging strategies. In effect, the stocks' future price volatility can rise because of a current lack of information about the extent to which dynamic hedging strategies are in place.


AB A corporation's securities provide the holder with particular claims on the firm's income stream and particular voting rights. These securities can be designed in various ways: one share of a particular class may have a claim to votes which is disproportionately larger or smaller than its claim to income. In this paper we analyze some of the forces which make it desirable to set up the corporation so that all securities have the same proportion of votes as their claim to income ("one share/one vote"). We show that security structure influences both the conditions under which a control change takes place and the terms on which
it occurs. First, the allocation of voting rights to securities determines which securities a party must acquire in order to win control. Secondly, the assignment of income claims to the same securities determines the cost of acquiring these voting rights. We will show that it is in shareholders’ interest to set the cost of acquiring control to be as large as possible, consistent with a control change occurring whenever this increases shareholder wealth. Under certain assumptions, one share/one vote best achieves this goal.


AB Recent advances in financial theory have created an understanding of the environments in which a real security can be synthesized by a dynamic trading strategy in a risk free asset and other securities. We contend that there is a crucial distinction between a synthetic security and a real security. In particular the notion that a real security is redundant when it can be synthesized by a dynamic trading strategy ignores the informational role of real securities markets. The replacement of a real security by synthetic strategies may in itself cause enough uncertainty about the price volatility of the underlying security that the real security is no longer redundant. Portfolio insurance provides a good example of the difference between a synthetic security and a real security. One form of portfolio insurance uses a trading strategy in risk free securities (“cash”) and index futures to synthesize a European put on the underlying portfolio. In the absence of a real traded put option (of the appropriate striking price and maturity), there will be less information about the future price volatility associated with current dynamic hedging strategies. There will thus be less information transmitted to those people who could make capital available to liquidity providers. It will therefore be more difficult for the market to absorb the trades implied by the dynamic hedging strategies. In effect, the stocks’ future price volatility can rise because of a current lack of information about the extent to which dynamic hedging strategies are in place.

Guasch, J. Luis
TI Heterogeneity, Tournaments, and Hierarchies. AU Bhattacharya, Sudipto; Guasch, J. Luis.

Guler, Kemal
ABSTRACTS

Hamilton, Jonathan H.
PD December 1987. TI Spatial Competition and the Core. AU Hamilton, Jonathan H.; MacLeod, W. Bentley; Thisse, Jacques Francois. AA Hamilton: University of Florida. MacLeod: Queen's University. Thisse: CORE, Universite Catholique de Louvain. SR Queen's Institute for Economic Research Discussion Paper: 704; Department of Economics, Queen's University, Kingston, Ontario, CANADA K7L 3N6. PG 27. PR Canada and United States $3.00; $3.50 foreign. JE 611, 022, 021. KW Spatial. Competition. Core. Differentiated Products. Duopoly. Nash Equilibrium. AB Models of spatial competition have proven to be very useful in describing differentiated products markets. A serious problem is that nonexistence of Nash equilibria seems endemic. This problem is resolved by modelling the price formation process using the core. The equilibrium is the outcome of a two-stage process. In the first stage, two firms choose locations simultaneously, looking ahead to the second stage. The second stage has prices determined by an allocation in the core of a cooperative subgame allowing for coalitions of buyers and sellers. The price selection is the joint profit maximum for the duopolists. This selection exists for all location pairs and coincides with the pure strategy Nash equilibrium of duopoly competition when the latter exists. Furthermore, these prices approach the competitive level as the distance between the firms goes to zero, thus capturing the essence of duopoly rivalry. For this price selection, in the location game, the two firms establish themselves at the efficient locations -- the first and third quartiles.

Hammitt, James K.
PD April 1987. TI Timing Regulations to Prevent Stratospheric-Ozone Depletion. AA The Rand Corporation. SR Rand Report: R-3495; The Rand Corporation, 1700 Main Street P.O. Box 2138, Santa Monica, CA 90406-2138. PG 62. PR No Charge. JE 613, 722, 022. KW Cost Analysis. Decision Framework. Policy Choices. AB Decisions concerning whether to impose regulations to restrict emissions of potential ozone-depleting substances must be made in a context characterized by three important features: (1) estimates of the likely extent of future stratospheric-ozone depletion and its consequences for life on earth are highly uncertain; (2) continuing scientific research can be expected to reduce, but not eliminate, these uncertainties; and (3) the relationship between potential-ozone-depleter production and environmental consequences is characterized by lags on the order of decades or more. Using a simple decision-tree framework, this research addresses the key question of whether it is desirable to impose emission-limiting regulations now, or to wait five to ten years to develop improved scientific understanding before deciding whether to regulate. Under a wide range of assumptions, beginning regulations immediately is cost-effective if the probability that regulations will eventually be required exceeds about 0.3 to 0.5.

Hammond, Peter J.
PD December 1986. TI The Power of Small Coalitions in Large Economies. AA Stanford University. SR Stanford Institute for Mathematical Studies in the Social Sciences (Economics Series) Technical Report: TR501; Institute for Mathematical Studies in the Social Sciences, Encina Hall, Fourth Floor, Stanford University, Stanford, CA 94305. PG 36. PR $4.00. JE 021. KW Core. Continuum Economy. Coalition. Limit Theorem. AB As long as coalitions eventually become large, the Debreu-Scarf limit theorem for the core holds even if coalitions are restricted in size so that their proportion of agents shrinks to zero as the economy becomes infinitely large. Corresponding results hold for non- replica economies. In a limiting continuum economy, the core equivalence theorem holds even if there must be a "measure-consistent" partition of a coalition into self-sufficient subcoalitions each with a finite number of agents. These results help relate standard results to those presented in collaboration with Kaneko and Wooders concerning finite coalitions in continuum economies.

Han, Aaron
PD November 1986. TI Semiparametric Estimation of Duration and Competing Risk Models. AU Han, Aaron; Hausman, Jerry. AA Han: Harvard University. Hausman: Massachusetts Institute of Technology. SR Massachusetts Institute of Technology Department of Economics Working Paper: 450; Department of Economics, Massachusetts Institute of Technology, Cambridge, MA 02139. PG 60. PR No Charge. JE 211, 212, 131. KW Duration Models. Unemployment. Proportional Hazards Model. Competing Risk Model. AB Since Lancaster's (1979) paper on unemployment, duration models have become commonly used in econometrics. In this paper, we specify and estimate a semiparametric proportional hazards (duration) model. The model specification is semiparametric in the sense that the baseline hazard is nonparametric while the effect of the covariates takes a particular functional form, which is typically linear although it need not be. The underlying hazard model is based on either an ordered probit or ordered logit model where an unknown parameter is estimated for each time interval over which the model is specified. A particular advantage of the specification is that the estimates of the parameters of the covariates are invariant to the length of time intervals which are chosen. Therefore, the grid of time intervals can be made finer as the sample size increases. We also add parametric heterogeneity to the underlying hazard model specification. The heterogeneity enters in extremely convenient form since the resulting model does not require numerical integration in estimation. In the sample of unemployed individuals examined in this paper, the addition of heterogeneity has very little effect on the results. Whether this finding is general to nonparametric baseline hazard specifications or is a particular finding for our sample, awaits future research.

Hardle, W.
TI On Bootstrapping Kernel Spectral Estimates. AU Franke, J.; Hardle, W.
Harris, Jeffrey E.
AB As of March 31, 1987, the United States Centers for Disease Control had reported 33,550 cases of acquired immune deficiency syndrome. Yet by that date, physicians had actually diagnosed 42,670 cases. The difference arises from significant delays in the reporting of Acquired Immune Deficiency Syndrome cases to public health authorities. An estimated 70 per cent of cases are reported two or more months after diagnosis; about 23 per cent are reported seven or more months later; and about 5 per cent take more than three years to come in. Moreover, the probability distribution of delays has been shifting to the right, with the median delay increasing by 0.6 months since mid-1986. From the data on reported cases and the estimated probability distribution of reporting delays, I reconstruct the actual incidence of AIDS from January 1982 through March 1987. The doubling time of the epidemic fell from about 6 months in 1982 to 15-16 months in 1986.

Harrison, Glenn W.
AB A number of recent studies have proposed, refined, extended and tested alternative noncooperative Nash equilibrium models of the behavior of first-price sealed-bid auctions with independent and private values. All of the existing tests have concentrated on deviations of subjects from predictions in the message space of auction: bid deviations. We suggest that it is more natural to evaluate subject behavior in expected payoff space. Certainly the latter is the appropriate metric to evaluate the incentives that subjects face in any experiment. What are indeed "statistically significant" deviations in terms of bids are not "statistically (or perceptually) significant" deviations in terms of foregone expected payoff. In brief, our reconsideration alters the metric of evaluation of the theoretical hypotheses in terms of the experimental results. We find that the experiments were not salient in terms of the inferences one would like to draw from them. We therefore conclude that the evidence against the proposed models is not significant enough to warrant their rejection.

AB The theoretical literature on the search behavior of workers and consumers typically considers three search strategies. These strategies are characterized by alternative assumptions about the temporal and temporal intensity of search. The first strategy, described by Stigler '1961, 1962, is the temporally intensive fixed-sample-size strategy (FSS) which restricts the agent to collecting exactly one sample of contemporaneous offers but allows him to choose the sample size. The second strategy, introduced by McCall '1970 and thoroughly reviewed by Lippman and McCall '1976, is the temporally intensive pure-sequential strategy (SEQ) which allows the agent to collect as many samples as he chooses but restricts the size of each to unity. The third strategy is the variable-sample-size strategy (VSS). This strategy is a generalisation of the first two since it allows the agent to sequentially choose both how many samples to take and the size of each sample. Descriptions of the VSS are given by Benhabib and Bull '1985, Gal, Landeberger and Levykson '1981, Morgan '1983 and Morgan and Mansing '1985. In this paper we report an experimental comparison and evaluation of these three search strategies.
AB Experiments are designed to test whether voluntary private provision of public goods meets theoretical expectations under the assumption of rational self-interested behavior. We go beyond the previous experimental literature in examining individual and group choices under alternative social composition functions, making explicit use of alternative decision protocols. For the sequential experiments, our results may be regarded as strongly confirming a compound hypothesis that the subjects: (a) acted in a rational, self-interested way, (b) believed that their partners would behave similarly, and (c) could learn the correspondence between their own and their partners' payoff functions. For the experiments conducted under the sealed-bid protocol, this compound hypothesis was less adequately confirmed. Further study will be necessary to specify which portions failed, and to what degree.

Hart, Oliver
PD February 1987. TI Contract Renegotiation and Coasian Dynamics. AU Hart, Oliver; Tirole, Jean.
AA Massachusetts Institute of Technology.
AB Consider a seller who wishes to sell a service to a buyer. If the seller doesn't know the buyer's willingness to pay for the service, he will set a price-quantity schedule in such a way as to screen for the buyer's valuation. An optimal price-quantity schedule will generally have the property that a buyer with a low willingness to pay will consume an inefficiently low amount of the service and may be shut out of the market altogether, even in cases where it is common knowledge that there are gains from trade. This one period nonlinear pricing or principal-agent problem has been the subject of much analysis and its solution is now well understood (see, e.g., Guesnerie-Laffont [1984] for a unified treatment and references). Much less attention, however, has been paid to dynamic extensions of the model, where trade is repeated over time. This paper is concerned with such an extension.

Haskel, Jonathan
AB This paper investigates some aspects of the growth in long-term unemployment in Britain from 1979 to 1986. It documents the behaviour of unemployment on the basis of a consistent series and suggests that the rise in long-term unemployment can be accounted for by a decline in the outflow rate from unemployment, both short-term and long-term, which took place during the 1980-81 recession, and has not subsequently been reversed. It also argues that special employment measures, in particular the Community Programme, have had a significant impact on long-term unemployment. The expansion in the Community Programme since 1983 has been associated with an increase in the outflow from unemployment of young people - those to whom the Community Programme had been primarily directed - but, it appears, a decline in the outflow rate of older people, suggesting there may be displacement effects at work.

Hatton, T. J.
AB Some 300 profit-sharing schemes were introduced in Britain between 1865 and 1913. These were intended both to raise labour productivity and to improve industrial relations in the firms concerned. These schemes appear to have increased significantly the wages of eligible workers not require one theory to understand the benefits and another to understand the costs.

TI One Share/One Vote and the Market for Corporate Control. AU Grossman, Sanford; Hart, Oliver D.

Hartmann, Mark
AB A topological characterisation is given for closed sets in Q(n) under the restriction of (cone) polar duality to Q(n).
but were frequently abandoned after an initial period of experiment. Analysis of data concerning these schemes indicates that the method of payment and the size of firm played important roles in the survival of the schemes, but that the probability of abandonment increased with the duration of the scheme.

Hausman, Jerry
TI Semiparametric Estimation of Duration and Competing Risk Models. AU Han, Aaron; Hausman, Jerry.

Helpman, Elhanan
AB Price controls were part of Israel's stabilization program of July 1985. Some results of the program seem to be inconsistent with competitive macroeconomic models. It is suggested that these results are consistent with an economy that has an oligopolistic market structure. The paper explores the effects of market structure on macroeconomic performance in the presence and absence of price control.

Hendershott, Patric H.
AB This paper summarizes the impact of economic, social and demographic variables on household formations and home ownership in the 1960-85 period and uses this knowledge to forecast household formations, and their split between owners and renters, through the year 2000. High and low growth forecasts are reported, both with and without enactment of the Tax Reform Act of 1986. The forecasts are compared with those of others. Net household formations are expected to be robust through 1990 (above 1 1/2 million per year), but to tail off sharply in the 1990s (down to 1 million by 2000). Home ownership should rise slightly in the 1990s.

Henderson, Yolanda K.
TI The Marginal Excess Burden of Different Capital Tax Instruments. AU Fullerton, Don; Henderson, Yolanda K.

Hendricks, Ken
AB This paper studies the dynamics of the discovery process for oil and gas pools in the Alberta basin from 1950 to 1979. A costs of adjustment, rational expectations model is specified in which current and future returns from exploration are random, and the main source of the uncertainty is the amount of discoveries. The parameters are estimated from the stochastic Euler equation using the Generalized Methods of Moments estimator proposed by Hansen (1982). We find that, at the appropriate level of aggregation, there is a stable, quantifiable relationship between exploratory investment and returns which is consistent with optimizing behavior.

Hendricks, Ken
AB This paper studies adoption of a new technology as the outcome of a game of incomplete information. Each firm knows its own belief about the technology, but is not sure about its rivals' beliefs. The crucial distinction is between pessimistic types, which believe that the new technology is too costly to adopt, and optimistic types, which believe that adoption is profitable. In the unique equilibrium, optimistic types exploit their ability to build reputations for pessimism to achieve an implicit agreement in which both firms engage in preemptive adoption. This leads to a theory of adoption in which rents from delayed adoption are realized, and where ex post returns are not equalized across adoption times.

Henderson, Ken
AB The paper provides a complete characterisation of the Nash equilibrium outcomes for the War of Attrition when time is continuous and information is complete. It allows for asymmetric payoffs and an arbitrary time horizon. In addition to certain (asymmetric) pure strategy equilibria which always exist, we establish the conditions under which there is also a continuum of mixed strategy equilibria. These are most likely to exist when either the horizon is infinite or the game is symmetric.
ABSTRACTS


AB This paper examines federal auctions for drainage leases on the Outer Continental Shelf from 1959 to 1969. These are leases which are adjacent to tracts on which a deposit has been discovered. We find that the data strongly support the hypothesis that neighbor firms are better informed about the value of a drainage lease than nonneighbor firms, that neighbor firms coordinate their bidding decisions, and that both types of firms bid strategically in accordance with the Bayesian-Nash equilibrium model for first-price, sealed bid auctions with asymmetric information.

Hercowitz, Z.


Heyman, D. P.


AB Recent proposals have been made which would replace the usage-sensitive carrier access charge by a charge billed directly to end users. In 1986 NYNEX proposed a tapered tariff of this sort which, it was hoped, would reduce bypass of the NYNEX local exchanges. The FCC refused to approve the tariff. In this paper we compute the efficiency effects of the NYNEX tariff and use the insights of optional tariff theory to compute optional two-part tariffs which Pareto dominate the current carrier access charge. Our results suggest that NYNEX could increase profits from access substantially, relative to the level attained under the carrier access charge, without making any users worse off.

Higgins, Richard


Hildenbrand, Werner


AB The weak axiom of revealed preference for the market demand function is the most general condition on the consumption sector of a private ownership economy that by itself guarantees uniqueness of equilibria for a regular economy if no restriction on the production sector of the economy is imposed. Hence, as long as one does not restrict the form of the total production set, the crucial question for uniqueness of equilibria is whether one can expect the axiom to hold for a reasonably general class of consumption sectors. We shall analyse this question here for a class of consumption sectors which have a particular structure. There are some commodities (called pure factors of production) which are not consumed by any individual household but they are used as inputs in production. These pure factors of production are owned by the households and they derive income from it (see assumption 1). Many general equilibrium models in the literature are of this type. Under quite weak assumptions on the individual demand functions, we shall show that the market demand function of such consumption sectors "typically" does not satisfy the weak axiom of revealed preference.

Hirshleifer, Jack


Hodrick, Robert J.


AB This paper explores a new direction for empirical models of exchange rate determination. The motivation arises from two well documented facts, the failure of log-linear empirical exchange rate models of the 1970's and the variability of risk premiums in the forward market. Rational maximizing models of economic behavior imply that changes in the conditional variances of exogenous processes, such as future monetary policies, future government spending, and future rates of income growth, can have a significant effect on risk premiums in the
foreign exchange market and can induce conditional volatility of spot exchange rates. I examine theoretically how changes in these exogenous conditional variances affect the level of the current exchange rate, and I attempt to quantify the extent that this channel explains exchange rate volatility using autoregressive conditional heteroskedastic models.

Holmstrom, Bengt R.
AB The theory of the firm has long posed a problem for economists. While substantial progress has been made on the description and analysis of market performance, firm behavior and organisation have remained poorly understood. Typically, the firm has been treated in no more detail than the consumer; indeed, the standard textbook analysis of production corresponds closely to the analysis of consumption. In light of scale differences, equal treatment is plainly peculiar. The volume of trade within firms is probably of the same order as market trade. Large firms are substantial subeconomies of their own with thousands of participants. This alone warrants more attention to non-market modes of transaction. The nature of decision-making within firms is of a different kind than individual choice in markets. Firm members act as agents for their superiors rather than themselves. In the aggregate, firm behavior is the result of a complex joint decision process within a network of agency relationships. One can justly ask what forces ensure that the process will maximize profits as postulated in the neoclassical theory. Thus, the question of firm organisation is not an independent appendix to value theory. It could well have ramifications for market analysis.

Holtz, Eakin Douglas
AB In current discussions of tax reform in the United States, there is considerable controversy concerning the effects of allowing individuals to deduct state and local taxes when calculating their federal income tax liability. Recent econometric work has suggested that federal deductibility of state and local taxes has raised the proportion of these taxes — especially property taxes — in local budgets. This paper lends additional support to these earlier findings by showing that one channel through which deductibility leads to higher local property tax revenues is by increasing the rate of local property taxation. Specifically, we find that if deductibility were eliminated, the mean property tax rate in our sample of 82 communities would fall by 0.00715 ($7.15 per thousand dollars of assessed property), or 21.1 percent of the mean tax rate.

Hoque, Asraul
AB In this paper we have estimated the relationship between farm size and economic efficiency by applying a random coefficient model to the production function where the operational definition of efficiency is derived from the profit maximizing behavior of the farmer. In contrast to earlier studies, piece-wise regression has been used instead of single regression to find the relationship. It has been found that a farm size between 7 and 12 acres of land could be the most efficient in the context of Bangladesh agriculture. This has an important policy implication in connection with land ceiling and land redistribution in Bangladesh.

Horstmann, Ignatius J.
AB The existence of advertising beyond the date at which a new good is introduced is anomalous in the context of Nelson-type models of advertising. This paper presents a model of advertising, based on private information about product quality, that i) yields such recurrent advertising in equilibrium; ii) generates equilibrium relationships among product price, advertising and quality similar to those suggested by earlier work, and iii) offers other new testable implications. The formal structure is a two-period game of imperfect information, with the equilibrium concept being a refinement of perfect sequential equilibrium. An accessible introduction to the use and refinement of sequential equilibrium is provided; the power of such techniques for applied research is illustrated within the analysis of the advertising model.

Howard, David H.

AB Argentina's Austral Plan is used as a point of departure for the investigation of the role of exchange rate policy in a macroeconomic stabilisation program for a developing country. A model of a country like Argentina is developed and the relationship between the exchange rate and macroeconomic policy is derived. The paper next explores the implications of alternative macroeconomic policy strategies involving exchange rates. The framework provides a rough way of quantifying and making operational what is meant by "appropriate" fiscal and monetary policy in the context of a stabilisation program. Finally, some practical aspects of implementing an exchange-rate-oriented macroeconomic stabilization program are discussed.

Huber, Alan M.
TI Government Saving, Capital Formation and Wealth in the United States, 1947-1985. AU Boskin, Michael J.; Robinson, Marc S.; Huber, Alan M.

Huffman, Gregory W.
TI Investment, Capacity Utilisation and the Real Business Cycle. AU Greenwood, J.; Hercowitz, Z.; Huffman, Gregory W.

Ichihishi, Tatsuro

AB Given two side-payment games v and w, both defined for the same finite player-set N, general characterizations of the following two conditions are established: (A) For every y element C(w) there exists x element C(v) such that y <= x; and (B) There exist y element C(w) and x element C(v) such that y <= x. (Here C(v) denotes the core of v.) For certain classes of games, such characterizations are simplified. A new class of no-gap exact games is proposed; it is dual to Sharkey's concept of exact games with a large core. Given a no-gap exact game v and an exact game w, (A) holds true if v(S) - w(S) <= v(N) - w(N) for every S subset of N. If v is not a no-gap exact game, there exists an additive game w for which the last condition is satisfied, yet (A) is not true. Given convex games v and w, (B) holds true if w(S) + v(NS) <= v(N) for every S subset of N.

Innes, Robert D.

AB A Brannan Plan policy can yield positive social benefits in an economy with stochastic production and incomplete markets under conditions which are plausible for an agricultural commodity. This paper takes these results as a point of departure, asking whether production controls, both as an isolated policy and as one employed with a Brannan Plan, can have desirable welfare properties in such an economy. In a variety of cases, these controls are found to be both socially harmful in a single-policy context and socially beneficial in the presence of a target price/deficiency payment scheme. Further, when monitoring costs prevent direct control of production, the use of an indirect control — namely, land set-asides — is shown to yield ambiguous welfare effects in the presence of a Brannan Plan; however, a numerical example indicates that the allocational costs of land set-asides, exacerbated by slippage, outweigh the benefits of supply cutbacks for a wide range of parameter specifications.

Iwamura, Kakuko

AB We show the existence of a lexicographically optimal base of a submodular system with respect to a weight vector. We also show a greedy procedure to get it through an algebraic consideration.

Jackman, Richard

AB This paper sets up a simple model of a unionized economy and shows that the introduction of profit-sharing unambiguously reduces the unemployment rate. The result arises because unions are assumed to care about the employment of their members but cannot bargain over employment directly. Profit-sharing reduces the perceived cost, in terms of worker income foregone, of increasing employment in the firm. In the economy as a whole, the equilibrium unemployment rate falls.

TI Long-Term Unemployment and Special Employment Measures in Britain. AU Haskel, Jonathan; Jackman, Richard J.

Jacquemin, Alexis
TI A Note on Cooperative and Noncooperative R&D in
Duopoly. AU d'Aspremont, Claude; Jacquemin, Alexis.

Jasso, Guillermina
AB In this paper we have used Census data from 1900 and 1980 to examine and compare the behavior of the major common-language groups of the foreign-born with respect to their English-language investment behavior and locational choices. Our results indicated that in both 1980 and 1900, when a far larger proportion of the United States population was foreign-born and did not speak English, higher economic rewards were associated with knowledge of English, and rewards to English proficiency and location were linked such that costs of lack of English proficiency were smaller in areas with greater concentrations of persons speaking the same non-English native language. In part as a consequence, those foreign-born in 1900 and 1980 who expected to spend less time in the United States were less likely both to acquire English-language skills and to move to locations with lower proportions of individuals speaking the same language. We also found that in both time periods, the English-language proficiency of the children of immigrants appeared to be influenced in similar ways by the English skills of their parents, household resources and the community environment.

Johnson, Paul
AB This paper examines the viewpoint that the dependency of elderly people in modern Britain has been increased by state action and social change. It argues that ideas of "structured dependency" are based upon theoretical premises which promote a one-sided reading of the evidence. An analysis of the changing composition of the income of the elderly population shows that the fall in the labour force participation of older people and the increased importance of state pension income has not led to the marginalisation of the elderly, but has instead promoted increased financial independence and consumer power.

AB This paper reviews evidence that life-cycle saving became the norm in nineteenth-century America, with a consequent fall in fertility and rise in the rate of capital formation, and considers whether a similar transition to life-cycle saving can be observed in nineteenth-century Britain. Although there is extensive evidence of widespread saving by British workers, most of this saving did not fit a life-cycle pattern. Liquidity constraints forced British workers to borrow, buy on credit, save only for short-run ends, and abstain from long-run accumulation. The paper concludes that some of the apparent difference between the savings behaviour of British and American workers may be the result of a misreading of United States evidence, some may be due to differences in old-age welfare systems, but that the most plausible explanation is that the real income of British workers in this period was substantially below that of their American counterparts.

Joskow, Paul L.
AB A sample of coal contracts between electric utilities and coal suppliers is used to analyse mechanisms for determining prices in long term contracts. Alternative methods for determining prices in long term contracts are discussed and the actual adjustment mechanisms specified in a set of actual coal contracts presented. The vast majority of long term coal contracts use a base price plus escalation or cost-plus adjustment formula. Base price equations and subsequent transactions price equations are estimated. The analysis shows that on average long term contracts are flexible in the sense that prices adjust to major changes in the costs of supplying coal. However, some pricing rigidities are found which appear to reflect the economic conditions prevailing at the time the contracts were executed. Furthermore, some contracts track changes in market values very poorly.

AB This chapter discusses alternative approaches to measuring the effects of "economic regulation" and reviews...
the empirical literature employing these approaches. By "economic regulation" we refer to both direct legislation and administrative regulation of prices and entry into specific industries or markets. We follow conventional treatment in distinguishing economic regulation from a host of other forms of government intervention in markets, including "social regulation" of environmental, health and safety practices, antitrust policy, and tax and tariff policies.

Joyce, Theodore
TI A Cost-Effectiveness Analysis of Strategies to Reduce Infant Mortality. AU Corman, Hope; Joyce, Theodore; Grossman, Michael.

Judd, Kenneth L.
TI Strategic Incentive Manipulation in Rivalrous Agency. AU Fershtman, Chaim; Judd, Kenneth L.
TI Cooperation through Delegation. AU Fershtman, Chaim; Judd, Kenneth L.; Kalai, Ehud.

Judge, George
AB Within the context of an orthonormal linear statistical model and multivariate conventional and joint one sided tests, this paper is concerned with the use of power and pre-test risk functions in making decisions concerning the choice between tests in practice. The informational content of these criteria, for the particular testing problem at hand is contrasted and discussed.

Kalai, Ehud
TI Cooperation through Delegation. AU Fershtman, Chaim; Judd, Kenneth L.; Kalai, Ehud.

Kamien, Morton I.
TI Turnpike Properties in a Finite Horizon Differential Game; Dynamic Duopoly With Sticky Prices. AU Fershtman, Chaim; Kamien, Morton I.

Kamiya, Kazuya
AB It is well known that firms' profit maximizing behavior is inconsistent with the existence of equilibria in an economy with increasing returns to scale (or nonconvex) technologies. The main purpose of this paper is to show that if firms adopt price setting behaviors then, under certain assumptions, there exists an equilibrium even in an economy with nonconvex technologies. In addition, the method of the proof allows us to deduce a uniqueness condition.

Kalaba, Robert
AB Suppose an investigator obtains noisy observations on a process which he believes can be adequately described by a linear regression model with regression coefficients which evolve slowly over time. The actual dynamic equations governing the evolution of the regression coefficients are unknown, and are proxied by a smoothness prior. Residual dynamic and measurement errors are anticipated to be small, but are otherwise unrestricted. The investigator wishes to estimate the time-varying regression coefficients. A "flexible least squares solution" is proposed for this problem. The flexible least squares solution is defined to be the collection of all coefficient sequence estimates which attain the "residual efficiency frontier" -- i.e., which yield minimal squared residual measurement error and dynamic error sums, conditional on the given observations. A FORTRAN program is presented which implements the flexible least squares solution. The program has been extensively tested, and incorporates several validation checks that users can employ. Simulation experiments involving linear, quadratic, and sinusoidal motions in the true regression coefficients are briefly described. In each experiment the flexible least squares estimates accurately reflect the qualitative time-variation displayed by the true regression coefficients, despite noisy observations.

Kalaba, Robert
AB An economy is analysed in which production and consumption occur in two periods. Future production is subject to technological uncertainty. Investment for future production is debt-financed, and firms with unfavorable technologies may default. Perfectly competitive lenders offer loan contracts which specify both the lending rate (price) and the amount to be loaned (quantity). Existence
of a general competitive equilibrium is established. (Certain complications arise because the loan supply correspondence is not convex-valued.) Depending on the nature of the technological uncertainty (e.g. with multiplicative uncertainty), equilibrium loan contracts may be characterized by credit rationing.

Kaneko, Mamoru

AB In previous papers, we defined our model of an economy with a continuum of players and finite coalitions and its core, called the f-core. The problem of this paper is the meaning of the model from the viewpoint of large finite economies. We study the problem by exploring convergence, from finite to the continuum, of solutions and of structures. The solutions are approximate cores for the finite economies and the f-core for the continuum economy. The special aspect of convergence in structure is that relative sizes of permissible coalitions converge to zero and, correspondingly, permissible coalitions are finite in the continuum economy. This convergence is obtained in the context of private goods exchange economies with widespread externalities. In answer to our problem of the meaning of the model, we interpret the continuum economy and its f-core as a large finite economy in a converging sequence and its approximate core.

Kanemoto, Yoshitsugu
PD December 1987. TI The Ratchet Effect, the Market for Senior Workers, and Intertemporal Commitment. AU Kanemoto, Yoshitsugu; MacLeod, W. Bentley. AA Kanemoto: Institute of Socio-Economic Planning, University of Tsukuba. MacLeod: Department of Economics, Queen's University. SR Queen's Institute for Economic Research Discussion Paper: 703; Department of Economics, Queen's University, Kingston, Ontario, CANADA K7L 3N6. PG 27. PR Canada & U.S. $3.00; $5.50 foreign. JE 813, 824, 918, 026, 022. KW Contract. Ratchet. Older Workers. AB This paper studies the effect that a labor market for older workers will have on the ratchet effect. Even though we assume that the information on worker type that a firm obtains will not be transmitted to other firms, the presence of the ex post labor market eliminates the ratchet effect. We also compare the cases with and without the market for senior workers, which yields useful insights on differences between labor markets in the U.S. and Japan.

Karp, Larry S.
PD August 1987. TI Estimating Market Structure and Tax Incidence: The Japanese Television Market. AU Karp, Larry S.; Perloff, Jeffrey M. AA Department of Agricultural and Resource Economics, University of California, Berkeley. SR University of California at Berkeley Department of Agricultural and Resource Economics (CUDARE) Working Paper: 445; 207 Giannini Hall, University of California, Berkeley, CA 94720. PG 36. PR $7.20. JE 631, 921, 212, 421. KW Market Structure. Taxation. Television Prices. Oligopolistic Industries. Exports. AB The tax incidence falling on consumers depends on the market structure. While the effect of market structure on tax incidence has been examined theoretically, we are unaware of any empirical research in this area. This paper estimates market structure and tax incidence in the Japanese television market. We believe there are four
reasons why this research is useful. First, we demonstrate theoretically and empirically that tax incidences on consumers can and do exceed 100 per cent in oligopolistic industries. Second, that tax incidences exceed 100 per cent is of practical importance as well as academic interest, since tax incidence is important in determining whether dumping has occurred under United States law. Third, the incidence of the tax determines whether it pays for a firm to export substantial quantities. Fourth, we derive measures of market structure and test whether the Japanese television market is competitive, Nash-Cournot, or collusive.

Katchalski, M.
TI The Maximum Size of a Convex Polygon in a Restricted Set of Points in the Plane. AU Alon, N.; Katchalski, M.; Pulleyblank, W. R.

Katz, Avery
AB It is commonly alleged that a substantial proportion of lawsuits are frivolous and are filed only for their nuisance value. This paper models settlement bargaining in the presence of frivolous suits as a game of asymmetric information, where the plaintiff knows the true merits of his claim, and the defendant does not, apart from any inferences he can draw from the fact of suit. When there is free entry to the opportunity to make a frivolous claim, the profit from doing so is driven to zero, and the surplus from settlement bargaining is completely dissipated. Several policies dealing with frivolous suits are examined; it turns out that requiring a losing litigant to pay the expenses of the winner (the English rule) does not alleviate the problem, but introducing a refundable deposit does.

Katz, Barbara G.
AB We study a Centrally Planned Economy in which an identical consumer good is sold under different price and availability conditions on the official market (OM) and a "second economy" market (SEM). The model contains planners, managers and consumers. Planners set input allocations, output targets, number of enterprises and the bonus function. They also fix the price and the rate at which output is sold on the OM. Managers divide inputs between production for the OM and SEM to maximize expected utility of wealth, balancing incentives from the bonus function with the stochastic revenue of sales to the SEM. Consumers are expected utility maximizers who purchase the goods on the OM or the SEM. On the OM, excess demand exists at the non-Walrasian fixed price; delivery date is stochastic. The SEM offers immediate availability at a market-clearing price. Our solution concept involves the rational expectations of managers concerning the equilibrium price, the consistency of the ex ante probability of waiting time with the ex post decisions of consumers, and a market-clearing SEM. Under a set of assumptions we derive a closed form solution for price and supply on the SEM in terms of the other parameters. We investigate the comparative statics of our solution and find that the response of price and supply on the SEM to an increase in inputs, for instance, is not always of one sign and depends on policy parameters. Sufficient conditions for the existence of the SEM to increase the sum of the aggregate utility of consumers and the aggregate utility of managers are also established.

AB We derive conditions under which retailers find it profitable to use special purchase merchandise to implement strategic stockouts. In particular, consumer surplus must be sufficiently sensitive to price changes and bargain-hunting must be costly. We argue that these conditions are likely to be satisfied when retailers set relatively low gross margins on regularly-stocked items. Thus, it is not surprising that supermarkets, with their traditionally low gross margins, feel constrained by the unavailability rule that prohibits grocery store stockouts and are seeking its repeal. We also show that any retailer with the incentive to adopt a special purchase program would prefer to bypass the restriction of a fixed price on the regularly-stocked item. In the absence of the general legal restrictions against bait advertising, the special purchase regime would degenerate as prices are raised in search of higher profits. All consumers who enter the market for X under these conditions, i.e., Theta < Theta (g*), run the risk of being worse off ex post in this regime than they would be in either the special purchase or the single brand regime.

AB Consumers purchase a good on either a rationed or an equilibrating market. On the former for price p1 the
good is obtained instantly or with delay with probabilities \( P \) and \( 1-P \) respectively. On the latter the good is obtained instantly for \( P \geq 0 \). We define and derive the conditions for a rational expectations equilibrium for this problem.

Katz, Lawrence

TI Employee Crime, Monitoring and the Efficiency Wage Hypothesis. AU Dickens, William T.; Katz, Lawrence; Lang, Kevin; Summers, Lawrence.

Kennan, John

TI An Experimental Analysis of Bargaining and Strikes with One-sided Private Information. AU Forsythe, Robert; Kennan, John; Sopher, Barry.

King, Elizabeth

PD December 1986. TI Change in the Status of Women Across Generations in Asia. AU King, Elisabeth; Peterson, Jane; Adietomo, Sri M.; Domingo, Lits; Syed, Sabiha H. AA The Rand Corporation.

SR Rand Report: R-5399; The Rand Corporation, 1700 Main Street P.O. Box 2138, Santa Monica CA 90406-2138.

PG 92. PR No Charge. JE 121, 851, 917, 212, 023.

KW Developing Countries. Discrimination. Intergenerational Model.

AB This report addresses several questions about changes in the activities and status of women in Pakistan, Indonesia, and the Philippines. It discusses differences in patterns and trends in these changes across the three countries, and the ways the status of women has improved across generations of families. It examines the factors that explain the patterns in education levels, age at marriage, and the distribution of occupations in these countries. The analysis is based on family and individual data from the Asian Marriage Surveys, which were fielded in 1979-1980.

King, Maxwell L.

TI A Further Class of Tests for Heteroskedasticity. AU Evans, Merran A.; King, Maxwell L.

Kletzer, Kenneth

TI Trade Policy Under Endogenous Credibility. AU Engel, Charles; Kletzer, Kenneth.

Kling, Arnold


AB We examine the risk characteristics of each portion of Interest-Only/Principal-Only mortgage strips, present results of a valuation model of these securities, and examine market prices of both the interest-only and principal-only portions of mortgage pools. We show that IO/PO securities are highly sensitive to the prepayment behavior of the underlying mortgage pool. Because that behavior varies systematically with the interest rate, and because prepayments affect the values of IO and PO components in opposite ways, the interest-rate risk of strip securities can differ substantially from that of the underlying mortgage pool. The PO component has much longer duration than the underlying mortgage pool. In contrast, the IO component typically will have a negative duration, at least in ranges for which interest-rate movements induce meaningful changes in mortgage prepayment behavior. We also show how market prices of partially-stripped Mortgage-Backed Strips that are actively traded on secondary markets can be used to infer market values of pure IO/PO strips. Recent market data is fully consistent with the theoretical insights offered by our valuation model. When interest rates spiked last April, PO values fell far more dramatically than those of the underlying mortgage pool while IO values actually rose.

Knight, J. B.


SR Oxford Applied Economics Discussion Paper: 35; Institute of Economics and Statistics, St. Cross Building, Manor Road, Oxford OX1 3UL, ENGLAND.

PG 63. PR No Charge. JE 917, 841, 121, 812.


AB The South African labor market has traditionally been characterized by huge racial inequality, mainly the result of racial discrimination both 'prior to' and 'within' the market. However, there are reasons to expect the labour market to have become more integrated over the last decade. This study exploits cross-section data sets for 1976 and 1985 which contain information on race, sex and job-evaluated skill. Mean earnings differences among races and over time are decomposed to examine the causes of inequality and its reduction via integration of the wage determination process and via job advancement. Both mechanisms are found to have operated, although considerable inequality still remains.

Koford, Kenneth


SR Caltech Social Science Working Paper: 635; Division of Humanities and Social Sciences, 228-77, California Institute of Technology, Pasadena, CA 91125.


AB While dimensional studies of legislative voting find a single ideological dimension (Schneider 1979, Poole and Rosenthal 1985b), regression estimates find constituency and party dominant (Kau and Rubin 1979, Peltzman 1984), and ideology secondary (Kalt and Zupan 1984). This paper rescales the dimensional findings to show their improved classification success over the null hypothesis that votes are not unidimensional. With the rescaling, most votes are not explained by one dimension, and
several dimensions are important. Nevertheless, fewer dimensions are found than constituents' preferences suggest. Thus a model is developed where transactions costs of building coalitions reduce the number of dimensions. When legislative parties build internal coalitions to pass and defeat bills, voting on randomly drawn bills has a single party-oriented dimension. And natural ideological dimensions are reinforced if parties write bills and logroll along natural lines of cohesion.

Korte, B.
TI Examples and Algorithmic Properties of Greedoids.
AU Goecke, O.; Korte, B.; Lovasz, L.

Kotlikoff, Laurence
AB This paper presents some preliminary findings about contact between the aged and their children based on a new survey of the aged and their children, entitled The Hebrew Rehabilitation Center for the Aged-National Bureau of Economic Research (HRC-NBER) Child Survey. Data on extended families is quite limited. The HRC-NBER Child Survey represents one of the few attempts to collect economic and demographic data on the elderly and their children. While these data will be used in future research to test structural models of the living arrangements, the purposes of the current paper are to describe the survey and to examine contact between the elderly and their children.

Kreps, David M.
TI On the Robustness of Equilibrium Refinements.
AU Fudenberg, Drew; Kreps, David M.; Levine, David K.

Krueger, Alan B.
AB This paper performs a longitudinal comparison of public and private sector pay. Although not decisive because of small sample sizes, the results tend to corroborate the conclusions of previous cross-sectional studies. Specifically, I find that on average wages of federal workers exceed those of private sector workers by 10 per cent to 25 per cent, while wages of state and local government workers are roughly equivalent to or slightly less than the wages of private sector workers. Furthermore, these conclusions hold for a sample of workers who joined the government after being involuntarily displaced from their private sector jobs. In addition, a comparative analysis of the length of job queues suggests that on average more workers apply for job openings in the federal government than in the private sector. Finally, both longitudinal and cross-sectional analyses support the conclusion that the union wage gap is substantially smaller in the public sector than in the private sector.

Krugman, Paul
AB There is a widespread view that world payments imbalances can be remedied through increased demand in surplus countries and reduced demand in deficit countries, without any need for real exchange rate changes. In fact shifts in demand and real exchange rate adjustment are necessary complements, not substitutes. The essential reason for this complementarity is that a much higher fraction of a marginal dollar of United States than of foreign spending falls on United States output. As a result, a redistribution of world spending away from the United States leads to an excess supply of United States goods unless accompanied by a decline in their relative price. Although some economists believe that the integration of world capital markets somehow eliminates this problem, this is a fallacy that confuses accounting identities with behavior. The paper also addresses a number of related issues, such as the role of budget deficits in determining domestic demand and the effectiveness of nominal exchange rates changes in producing real depreciation.
Kuhn, Peter
PD April 1987. TI Social Security, Longevity, and Moral Hazard. AU Kuhn, Peter; Davies, James B. AA Department of Economics, University of Western Ontario. SR University of Western Ontario Department of Economics Research Report: 8706; Department of Economics, Social Sciences Center, University of Western Ontario, London, Ontario, CANADA N6A 5C2. PG 42. PR $5.00 Canada; $7.00 Elsewhere. JE 915, 918, 915.

AB Analysis of the impact of government policy on longevity is illustrated for the social security system, using a simple theoretical model. Recent literature has considered how adverse selection in annuity markets provides a rationale for social security, but has ignored the moral hazard involved, that is induced changes in behavior tending to increase longevity. Here individuals consume a health-related good which may either increase or reduce longevity. A competitive annuity market in the absence of government is characterized, and then actuarially fair social security is introduced. In this setting social security is never welfare-improving. In most cases it tends to encourage longevity, whereas it is shown that there is an optimal Pigouvian subsidy on products, like cigarettes, which reduce longevity in this model. Private agents ignore the external effect of their health investments in raising premia in competitive annuity markets. A subsidy to cigarettes, or taxes on healthful commodities may correct this distortion.

Kulchycky, Ksenia
TI U.S. and Swedish Direct Investment and Exports. AU Blomstrom, Magnus; Lipsey, Robert E.; Kulchycky, Ksenia.

Lach, Saul

AB This paper analyses the interaction among R&D, capital investment, and the stock market rate of return for 191 firms in science-based industries for the period 1973-1981. Using a framework based on dynamic factor analysis, we show how several prominent hypotheses about the determination of R&D and investment generate testable parameter restrictions. The data indicate that R&D Granger-causes investment, but that investment does not Granger-cause R&D. We use this finding to examine the validity of these hypotheses, to characterize the movements over time of R&D and investment, and to measure the stock market valuation of these movements.

Laidler, David E. W.

AB This paper compares two bodies of business cycle theory that built upon the work of Kunt Wickssel, considers the reasons for the differences between them, and assesses their influence on the development of macroeconomics.

Landa, Janet T.

AB The transaction cost approach to the study of organizations has identified two alternative organizational modes or governance structures in developed capitalist economies -- markets vs. hierarchies -- for coordinating the economic activities of interdependent firms. When attention is shifted to developing economies, the phenomenon of personalistic exchange networks embedded in the ethnically-homogeneous middleman group (EHMG) reveals itself to be the dominant form of economic organization for coordinating the activities of middlemen across markets. Coordinating of middlemen activities is achieved via the role of informal norms of behavior embedded in personalistic exchange networks. Thus, in addition to markets and hierarchies, personalistic exchange networks/ehmg, which as an organizational mode is neither market nor hierarchy, must be considered a third form of economic organization. The paper develops a theory of the EHMG as a club-like organization for economizing on costs of contract enforcement, drawing on various key concepts in the social sciences.

Lang, Kevin
TI Employee Crime, Monitoring and the Efficiency Wage Hypothesis. AU Dickens, William T.; Katz, Lawrence; Lang, Kevin; Summers, Lawrence.

TI A Goodness of Fit Test of Dual Labor Market Theory. AU Dickens, William T.; Lang, Kevin.

Laroque, Guy


AB The transaction cost approach to the study of organizations has identified two alternative organizational modes or governance structures in developed capitalist economies -- markets vs. hierarchies -- for coordinating the economic activities of interdependent firms. When attention is shifted to developing economies, the phenomenon of personalistic exchange networks embedded in the ethnically-homogeneous middleman group (EHMG) reveals itself to be the dominant form of economic organization for coordinating the activities of middlemen across markets. Coordinating of middlemen activities is achieved via the role of informal norms of behavior embedded in personalistic exchange networks. Thus, in addition to markets and hierarchies, personalistic exchange networks/ehmg, which as an organizational mode is neither market nor hierarchy, must be considered a third form of economic organization. The paper develops a theory of the EHMG as a club-like organization for economizing on costs of contract enforcement, drawing on various key concepts in the social sciences.

Laroque, Guy

AB This paper reviews the recent work on the theory of the business cycle, focussing on the behavior of inventories during the cycle. The paper is organised as follows. First some of the basic stylised facts, i.e. the relationship between the growth rate of GNP and the second difference in the levels of inventories, are recalled. Second, the role of inventories in rational expectations competitive models of the cycle is discussed, both in deterministic and stochastic setups. Finally, the third section describes some recent work in the Keynesian tradition, in a deterministic framework. In particular, a perfect foresight version of a Keynesian model is suggested, where speculative inventory behavior is destabilising.

TI Asset Pricing and Optimal Portfolio Choice in the Presence of Illiquid Durable Consumption Goods.

AU Grossman, Sanford; Laroque, Guy.


AB The payoff structure of Las Vegas slot machines, the timing of evaluations and raises in the labor market, and the repayment structure of loans have many common elements. It is argued that frequent payments provide additional information to gamblers, workers, and lenders. These agents are willing to pay for the information. That rather obvious point yields a number of implications about the structure of labor and financial markets. The theory is essentially one of endogenous time preference and is akin to the psychologist's notions of reinforcement.


AB European countries have enacted various job security provisions over the last thirty years. Employers are required to pay workers on separation and/or to give advance notice of termination. In anything less than a perfectly functioning market, there are effects of the provisions on employment. Incumbents are more likely to retain their jobs, but new workers are less likely to be hired. An examination of the European data reveals that severance pay requirements reduce employment substantially. The main effect of notice provisions appear to be a reduction in hours worked, as firms switch from covered full-time, permanent workers to exempted part-time, temporary workers.

Lazorchak, J. M.

TI An Analysis of Tapered Access Charges for End Users. AU Heyman, D. P.; Lazorchak, J. M.; Sibley, D. S.; Taylor, W. E.


AB Much of the theoretical basis for current monetary and financial theory rests on the economic efficiency of financial markets. Not surprising, considerable effort has been expended to test the efficient markets hypothesis, usually by examination of the predictability of equity returns. Unfortunately, there are two competing explanations of the presence of such predictable variation: (1) market inefficiency and stock price 'overreaction' due to speculative 'fads' and (2) predictable changes in expected security returns associated with forecasted changes in market or individual security 'fundamentals.' These explanations can be distinguished by examining equity returns over short time intervals since there should be negligible changes in the fundamental valuation of individual firms over intervals like a week in an efficient market. This study finds sharp evidences of market inefficiency in the form of systematic tendencies for current winners' and 'losers' in one week to experience sizeable return reversals over the subsequent week in a way that reflect apparent arbitrage profits. These measured arbitrage profits persist after corrections for the mismeasurement of security returns because of thin trading and bid-ask spreads and for plausible levels of transactions costs.


AB This paper examines the validity of the APT based on maximum likelihood factor analysis of large cross-sections. Our empirical implementation proves incapable of explaining expected returns on portfolios with different market capitalisations although it provides an adequate account of the expected returns of portfolios formed on the basis of dividend yield and own variance where risk adjustment employing the usual CAPM market proxies fails. We also compare alternative versions of the APT and sharply reject the hypothesis that basis portfolios
formed to mimic the factors span the mean-variance frontier of the individual assets.

Lehrer, Ehud
TI Regular Simple Games. AU Einy, Ezra; Lehrer, Ehud.

Leijonhufvud, Axel
PD September 1986. TI Whatever Happened to Keynesian Economics? AA Department of Economics, University of California, Los Angeles. SR University of California at Los Angeles Department of Economics: 419; Department of Economics - University of California at Los Angeles, Los Angeles, CA 90024. PG 25. PR $2.50. JE 031, 023. KW Keynes. Economic Thought. AB The loss of influence of Keynesian economics is discussed in terms of external and internal developments. On the external side, the postwar evolution of the monetary system led in the seventies to a discretionary flat regime, which would not generate the stickiness of nominal magnitudes characteristic of much Keynesian theorizing. On the internal side, Keynesian economics suffered from a number of conceptual problems and theoretical confusions that were not adequately dealt with in the period of Keynesian predominance. Amongst these, one confusion seems particularly important, namely the shift of focus from the real intertemporal (saving-investment) disequilibrium of Keynes to the nominal (money stock-money wage rule) disequilibrium of later Keynesians.

Levine, David K.
TI Finite Player Approximations to a Continuum of Players. AU Fudenberg, Drew; Levine, David K.
TI On the Robustness of Equilibrium Refinements. AU Fudenberg, Drew; Kreps, David M.; Levine, David K.

Levy, Anat
PD January 1988. TI An Economic Evaluation of Lock vs. No-Lock Mortgage Plans: A Queuing Analysis. AU Levy, Anat; Levy, Hanoch. AA Levy, Anat: Department of Economics, Tel-Aviv University. Levy, Hanoch: Department of Computer Sciences, Tel-Aviv University. SR Tel-Aviv Foerder Institute for Economic Research Working Paper: 7-88; Department of Economics, Tel-Aviv University, Ramat Aviv 69978, Tel-Aviv, ISRAEL. PG 19. PR No Charge. JE 312, 026, 022. KW Price Locking Policy. Queuing. Mortgage Plans. Optimal Pricing. AB Mortgage prices are determined according to two major alternative plans: One is the Lock Plan (LP), in which the price is determined at time of application, and the other is the No-Lock Plan (NLP), in which the price is determined when the application process ends and mortgage commitment is issued. It is widely believed that the difference between the plans is mainly due to risk shifting between borrowers and lenders. By constructing a queuing model to represent the mortgage system and analyzing the optimal pricing policy for the two plans, we show, however, that even if risk factors are controlled, there exist inherent differences between the plans. In particular, when the optimal policy is utilized, the NLP consistently yields higher revenues than the LP. The ability of lenders to regulate the queue size by varying prices, combined with their ability to change the price spread while customers are already in the queue, generates those extra revenues. The relevance of these results to policy application is discussed.

Levy, Hanoch

Lewis, Alain A.

Lewis, Tracy R.
PD April 1987. TI Regulating a Monopolist with Unknown Demand and Cost Functions. AU Lewis, Tracy R.; Sappington, David E. M. AA Bell Communications Research, Inc. SB Bell Communications Research Inc Economics Discussion Paper: 36; Bell Communications Research, Incorporated
ABSTRACTS


AB We consider the design of regulatory policy when the regulator is imperfectly informed about both the firm's cost function and the demand function it faces. To some extent, the optimal policy is the natural "combination" of the policies when there is uncertainty about demand alone or cost alone. But important qualitative differences also exist. For example, prices may optimally be set below marginal cost when there is uncertainty about both cost and demand, although prices will never fall below marginal cost when there is only a single source of uncertainty, whether it pertains to cost or demand.


AB We analyze the design of regulatory policy when the firm has better information about demand than the regulator from the outset of their relationship. Such a situation is likely to arise, for example, when demand is determined by the quality or reliability of the good or service being offered, and the regulator cannot measure these characteristics at the time production takes place. We assume that the firm's cost structure is common knowledge and that monitoring of output is prohibitively costly. We find that when marginal costs of production increase with output, the firm can command no rents from its private information, and the first-best policy is feasible. In contrast, with declining marginal costs, a single price is always optimal under plausible assumptions about the relevant information asymmetry. Thus, major qualitative differences in the optimal regulatory policy arise when the firm's private information concerns demand rather than costs.


AB We examine the implications of countervailing incentives in agency problems. Such incentives exist when the agent has an incentive to understate his private information for some of its realizations, and to overstate it for others. Countervailing incentives alter the qualitative properties of the equilibrium contract. In particular, pooling generally arises, and efficient performance is induced at an intermediate as well as both extreme realizations of the underlying private information. Also, the agent's rents will generally increase with the realization of his private information over some ranges, and decrease over other ranges. Performance will also be distorted both above and below efficient levels.

Lindsey, Robin
TI Bottleneck Congestion with Elastic Demand. AU Arnott, Richard; de Palma, Andre; Lindsey, Robin.

Lipsey, Robert E.
TI U.S. and Swedish Direct Investment and Exports. AU Blomstrom, Magnus; Lipsey, Robert E.; Kulchycky, Kenia.

Lovasz, L.
TI Examples and Algorithmic Properties of Greedoids. AU Goecke, O.; Korte, B.; Lovasz, L.
Love, James P.  
TI The Real Exchange Rate and Employment in U.S. Manufacturing: State and Regional Results.  
AU Branson, William H.; Love, James P.

Lyon, Andrew B.  
TI Tax Neutrality and Intangible Capital.  
AU Fullerton, Don; Lyon, Andrew B.

MacDonald, Glenn M.  
TI Recurrent Advertising.  
AU Horstmann, Ignatius J.; MacDonald, Glenn M.

Mackie, Mason Jeffrey K.  
PD August 1987.  
TI Taxes, Information and Corporate Financing Choices.  

AB The paper uses a different approach from most capital structure studies, and a large new data set to study many hypotheses of the determinants of financial decisions. We focus on incremental financing choices by firms (new public issues) rather than the debt/assets ratio. We resolve some questions about the role of taxes, by obtaining strong and plausible results after controlling for confounding effects which have been ignored in previous studies. We also find strong support for several predictions of moral hazard and financial distress theories of optimal leverage ratios. Some evidence of signaling costs for equity issues emerges, but the extreme "pecking order" hypothesis (that firms have hierarchical preferences with no optimal debt ratio) is rejected.

MacKinnon, James  
TI Double-Length Artificial Regressions.  
AU Davidson, Russell; MacKinnon, James.

TI Testing for Consistency Using Artificial Regressions.  

AB We consider several issues related to what Hausman '1978 called "specification tests", namely tests designed to verify the consistency of parameter estimates. We first review a number of results about these tests in linear regression models, and present some new material on their distribution when the model being tested is false, and on a simple way to improve their power in certain cases. We then show how in a general nonlinear setting they may be computed as "score" tests by means of slightly modified versions of any artificial linear regression that can be used to calculate Lagrange Multiplier tests, and explore some of the implications of this result. In particular, we show how to create a variant of the information matrix test that tests for parameter consistency. We examine both the conventional information matrix test and our new version in the context of binary choice models, and provide a simple way to compute both tests based on artificial regressions. Some Monte Carlo evidence is also presented; it suggests that the most common form of the information matrix test can be extremely badly behaved in samples of even quite large size.

MacLeod, Bentley  
TI Labour Turnover and the Natural Rate of Unemployment: An Incomplete Contracts Approach.  
AU MacLeod, W. Bentley; Malcomson, James M. AA MacLeod: Queen's University. Malcomson: University of Southampton. SR Queen's Institute for Economic Research Discussion Paper: 697; Department of Economics, Queen's University, Kingston, Ontario, CANADA K7L 3N6. PG 32. PR Canada & U.S. $5.00; $5.50 foreign. JE 921, 029. KW Incomplete Contracts. Unemployment. Turnover. Dynamic Model.

AB The purpose of this paper is to study the effect of incomplete contracts on the level of unemployment in a dynamic model with endogenous turnover. First it is shown that if effort is non-contractable, then this will lead to wages above the market clearing level. Secondly, as the level of uncertainty in the economy increases, this will lead to greater turnover, higher wages, and lower output.

PD December 1987.  
TI Price Discrimination and Equilibrium in Monopolistic Competition.  

AB Modern theories of monopolistic competition have borrowed extensively from techniques developed in location theory and the theory of spatial pricing: the monopolistically competitive firm is assumed to choose a "location" and price for its product. A subject that has been of increasing concern in this corpus of theory is that there exists no free-entry price-location equilibrium. In this paper we demonstrate that free-entry price-location equilibrium exists provided only that producers are allowed to price discriminate among customers in a reasonable manner. Equilibrium is modelled as a two-stage game using the Selten concept of subgame perfect Nash equilibrium. It is shown that the equilibrium discriminatory price system is one initially identified by Hoover. In addition, we show that equilibrium is not unique. The precise nature of equilibrium in a particular market will be dependent upon the history of that market.

TI Price Discrimination and Product Line Rivalry.  
AU Ginsburgh, Victor; MacLeod, Bentley; Weber, Shlomo.

TI The Ratchet Effect, the Market for Senior Workers,
and Intertemporal Commitment. AU Kanemoto, Yoshitugu; MacLeod, W. Bentley.

TI Spatial Competition and the Core. AU Hamilton, Jonathan H.; MacLeod, W. Bentley; Thisse, Jacques Francois.

TI Price Discrimination and Product Line Rivalry. AU Ginsburgh, Victor; MacLeod, Bentley; Weber, Shlomo.

Magill, M.

Mahjoup, Ali Ridha
TI Compositions of Graphs and Polyhedra II: Stable Sets. AU Barahona, Francisco; Mahjoup, Ali Ridha.

Malcomson, James M.
TI Labour Turnover and the Natural Rate of Unemployment: An Incomplete Contracts Approach. AU MacLeod, W. Bentley; Malcomson, James M.

Mankiw, Gregory
TI The Worldwide Change in the Behavior of Interest Rates and Prices in 1914. AU Barsky, Robert; Mankiw, N. Gregory; Miron, Jeffrey; Well, David.

TI The Worldwide Change in the Behavior of Interest Rates and Prices in 1914. AU Barsky, Robert B.; Mankiw, N. Gregory.

AB This paper presents a simple general equilibrium model in which the only non-Walrasian feature is imperfect competition in the goods market. The model is shown to exhibit various Keynesian characteristics. In particular, as competition in the goods market becomes less perfect, the fiscal policy multipliers approach the values implied by the textbook Keynesian cross.

TI Permanent Income, Current Income and Consumption. AU Campbell, John Y.; Mankiw, Gregory N.

Marcus, Alan J.
TI Interest-Only/Principal-Only Mortgage-Backed Strips: A Valuation and Risk Analysis. AU Kling, Arnold; Marcus, Alan J.

Martin, Lawrence
TI Optimal Labor Market Policies with Search Unemployment. AU Davidson, Carl; Martin, Lawrence; Matusz, Steven.

Maschler, Michael
AB A dynamic system is constructed to model a possible negotiation process for players facing a (not necessarily convex) pure bargaining game. The critical points of this system are the points where the "Nash product" is stationary. All accumulation points of the solutions of this system are critical points. It turns out that the asymptotically stable critical points of the system are precisely the isolated critical points where the Nash product has a local maximum.

Matusz, Steven
PD October. TI Optimal Labor Market Policies with Search Unemployment. AU Davidson, Carl; Martin, Lawrence; Matusz, Steven.

Matzkin, Rosa L.
AB We prove that the Strong Axiom of Revealed Preference tests the existence of a strictly quasiconcave (in fact, continuous, generically C(infinity) strictly concave, and strictly monotone) utility function generating finitely many demand observations. This sharpeners earlier results of Afriat, Diewert, and Varian that tested ("nonparametrically") the existence of a piecewise linear utility function that could only weakly generate those demand observations. When observed demand is also invertible, we show that the rationalising can be done in a C(infinity) way, thus extending a result of Chiappori and Rochet from compact sets to all of R(n). For finite data sets, one implication of our result is that even some weak types of rational behavior -- maximisation of pseudotransitive or semitransitive preferences -- are observationally equivalent to maximisation of continuous, strictly concave, and strictly monotone utility functions.

Mayer, Thomas
PD November 1987. TI Minimizing Regret as an Explanation of Fed Policy: An Application of Cognitive Dissonance Theory. AA University of California at Davis. SR University of California at Davis Research Program in Applied Macro and Macro Policy: 49; Department of Economics, University of California at Davis, Davis, CA 95616. PG 23. PR No Charge. JE 311. KW Monetary Policy. FOMC. Cognitive
Dissonance.
AB The policy-maker is assumed here to minimize regret by avoiding policies where errors will become apparent. This is based on a Thaler–Shefrin type utility function and on cognitive dissonance theory. It helps to explain certain characteristics of Fed behavior, such as the Fed's tendency to stick with its policies, its relative neglect of the problem of lags in monetary policy, and its preference for an interest-rate target over a money target.

McCulloch, J. Huston
TI The Term Structure of Interest Rates. AU Shiller, Robert J.; McCulloch, J. Huston.

McDermied, Ann
AB This study estimates the magnitude of pension wealth and compares pension wealth to net worth for households in the 1983 Survey of Consumer Finance (SCF). The SCF is the first data set to provide detailed information on both household finances and pension characteristics. The pension information is provided by the employer, so that it is much more detailed and likely to be more accurate than the pension data used in previous studies. Pension wealth was estimated under two sets of assumptions. Under the projected earnings approach, mean pension wealth is $98,291, which represents 43 percent of mean net worth for households with pensions. Under the legal method of calculating pension wealth, mean pension wealth is $47,541, which represents 26 percent of mean net worth for households with pensions. Both estimates are much larger than those obtained in earlier studies. The study also examines how estimates of inequality in the wealth distribution change when pension wealth is added to household balance sheets. Using a variety of methods and assumptions, the distribution becomes more equal when the definition of wealth is expanded to include pension assets.

McGrath, M. D.
TI The Erosion of Apartheid in the South African Labor Market: Measures and Mechanisms. AU Knight, J. B.; McGrath, M. D.

McKee, Michael
TI Can the Private Provision of Public Goods be Efficient? — Some Experimental Evidence. AU Bagnoli, Mark; McKee, Michael.

McKelvey, Richard
AB The Euclidean representation of political issues and alternative outcomes, and the associated representation of preferences as quasi-concave utility functions is by now a staple of formal models of committees and elections. This theoretical development, moreover, is accompanied by a considerable body of experimental research. We can view that research in two ways: as a test of the basic propositions about equilibria in specific institutional settings, and as an attempt to gain insights into those aspects of political processes that are poorly understood or imperfectly modeled, such as the robustness of theoretical results with respect to procedural details and bargaining environments. This essay reviews that research so that we can gain some sense of its overall import.

McMillan, John
AB Consider an oligopolistic industry in which the firms produce perfect substitutes and incur transaction costs of changing price. Under constant inflation, there is an equilibrium in which the firms change their nominal prices at equally spaced time-points. Increasing the inflation rate increases the size of price changes, increases the frequency of price changes, and increases the average real price paid by buyers. The analysis derives its significance from its implications for the welfare costs of inflation: the inflation-induced distortions in relative prices are larger the more sticky nominal prices are; and are larger the greater the tendency for firms to stagger (rather than synchronize) their price changes.

Meese, Richard
AB In this paper we explore the relationship between real exchange rates and real interest rate differential for the United States, Germany, Japan and the United Kingdom. Contrary to theories based on the joint hypothesis that domestic prices are sticky and monetary disturbances are
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predominant, we find little evidence of a stable relationship between real interest rates and real exchange rates. We consider both in-sample and out-of-sample tests. One hypothesis which is consistent with our findings is that real disturbances (such as productivity shocks) may be a major source of exchange rate volatility.

Mehta, J. S.
AB Multicollinearity presents a real problem if the population values of insignificant coefficients are, in fact, not zero and the reason that these coefficients turn out to be insignificant is that approximate linear relations hold among the observed values of the regressors. The appearance of these approximate linear relations points to only apparent multicollinearity if the population values of the coefficients corresponding to the nonorthogonal observation vectors of regressors are all zero. Any diagnostic measure that depends on the matrix of observations on the regressors alone cannot take into account the value of coefficients and, therefore, cannot enable us to distinguish real multicollinearity from apparent multicollinearity. While there is no completely reliable way of detecting real multicollinearity, the measure of multicollinearity employed by Theil, unlike other measures suggested by numerical analysts and statisticians, does not ignore the sample information about coefficients. In this paper, we give numerical tables of the exact cumulative distribution function of Theil's measure in the normal case to show that the distribution is tighter and centered at correct values when there is a high degree of real multicollinearity.

Mertens, Jean Francois
AB T.U. economies with private production are shown to have a value - as defined in Mertens '1983 - without any differentiability or interiority or other restriction. An explicit formula is given, describing the value as a barycenter of the Core, for a probability distribution depending only on the set of net trades at equilibrium.

Miron, Jeffrey A.
AB We prove here a measurable version of the measurable choice theorem (a.o., basically of Lyapunov's theorem), in the sense that the measurable selection (the set) can be chosen in a measurable way as a function of the underlying probability measure, of the integral (measure) desired, and of the correspondence itself.

AB We prove the existence of subgame perfect equilibria for discounted stochastic games with general state and action sets, using minimal assumptions (measurability as a function of states, and for each fixed state, compactness of action sets and continuity on those) - except for the rather strong assumption that the transition probabilities are norm-continuous functions of the actions.

Mintz, Jack M.
AB In the Fall of 1985 the John Deutsch Institute for the Study of Economic Policy, in cooperation with the Department of Finance (Canada), mounted a conference on Taxation and Business Activity. This survey was written as an introduction to the conference volume which will be published in November 1987 by the JDI. Focus is on the behavioral analysis of business decisions -- in particular on production, investment, and financing decisions -- and on the available evidence concerning the importance of various determinants of these activities. The four surveys written for the volume provide a detailed description of the current state of knowledge for specialists in the area of tax policy. Each survey outlines theoretical and empirical issues that arise in the study of the effects of taxes on business activity. Since the subject matters of the four surveys are closely related, there are a number of important themes common to them. In this introductory essay we develop some of these common themes.
The first measure, which we refer to as IP, is the index of industrial production constructed by the Board of Governors of the Federal Reserve. This measure is used extensively in empirical work on the business cycle, as well as by policymakers and others to assess the current state of the economy. The second measure, which we refer to as Y4, is constructed from the accounting identity that estimates models of inventory accumulation. Theoretically, these two series measure the same underlying economic variable—the production of goods by firms during the month. We show here that the time series properties of these two series are radically different. We examine means, variances, and serial correlation coefficients of the log growth rates, and show that these statistics differ substantially between the two series. In addition, the cross-correlations between the two seasonally adjusted series range from .7 to .0 and are in most cases less than .4. We then demonstrate the significance of these differences in two ways.

TI: The Seasonal Cycle and the Business Cycle. AU: Barsky, Robert B.; Miron, Jeffrey A.


AB: A great deal of research on the empirical behavior of inventories examines some variant of the production smoothing model of finished goods inventories. The overall assessment of this model that exists in the literature is quite negative: there is little evidence that manufacturers hold inventories of finished goods in order to smooth production patterns. This paper examines whether this negative assessment of the model is due to one or both of two features: costs shocks and seasonal fluctuations. First, we present a general production smoothing model of inventory investment that is consistent with both seasonal and non-seasonal fluctuations in production, sales, and inventories. The model allows for both observable and unobservable changes in marginal costs. Second, we estimate this model using both seasonally adjusted and seasonally unadjusted data plus seasonal dummies. The goal here is to determine whether the incorrect use of seasonally adjusted data has been responsible for the rejections of the production smoothing model reported in previous studies. The third part of our approach is to explicitly examine the seasonal movements in the data. We test whether the residual from an Euler equation is uncorrelated with the seasonal component of contemporaneous sales. Even if unobservable seasonal cost shocks make the seasonal variation in output greater than that in sales, the timing of the resulting seasonal movements in output should not necessarily match that of sales. The results of our empirical work provide a strong negative report on the production smoothing model, even when it includes cost shocks and seasonal fluctuations.

Mitchell, Olivia S.


AB: Most retirement studies examine older married couples in which the husband is the sole earner. This paper extends the focus of analysis to examine older dual-earner couples. It further evaluates the impact of Social Security reforms on older working couples' retirement ages and retirement incomes. Specifically, we examine two questions: (1) What are the likely effects of changes in Social Security rules on the retirement decisions of older working women and their husbands? and (2) How are these changes likely to alter the incidence of poverty among retired dual-earner couples? The evidence suggests that benefit reforms intended to bolster the Social Security Administration's financial position are also likely to worsen the economic status of an important minority of dual-earner couples.
Mohring, R.
TI Scheduling Project Networks with Resource Constraints and Time Windows. AU Bartusch, M.; Mohring, R. H.; Radermacher, F. J.


AB Ordered sets have recently gained much importance in many applied and theoretical problems in computer science and operations research ranging from project planning via processor scheduling to sorting and retrieval problems. These problems involve partial orders as their basic structure, e.g. as precedence constraints in scheduling problems, or as comparability relation among the objects to be sorted or retrieved. Since many of the involved problems are NP-hard in general, much attention has recently been given to special classes of partial orders with "nice" structural properties that lend themselves the design of efficient methods, and for obtaining bounds by structural relaxation in more general situations. Typical such classes are: series parallel partial orders, N-free partial orders, interval orders, two-dimensional partial orders, and partial orders with special decomposition properties. This area of "computationally tractable" classes of partial orders shows many similarities and interactions with algorithmic graph theory and certain classes of perfect graphs. We will present the structural properties of the mentioned classes, discuss their mutual relationship, and the algorithmic complexity of their recognition. In addition, we present the tractability of these different classes on several applications dealing with scheduling and sorting.

Morgon, Peter
TI Search Intensity in Experiments. AU Harrison, Glenn W.; Morgan, Peter.

Morris, John
TI How Much Care Do the Aged Receive from their Children? A Bimodal Picture of Contact and Assistance. AU Koslikoff, Laurence; Morris, John.

Negri, Donald

Nelson, R. H.; Radermacher, F. J.


AB Recent research has proposed the state space (SS) framework for decomposition of Gross National Product and other economic time series into trend and cycle components, using the Kalman filter. This paper reviews the empirical evidence and suggests that the resulting decomposition may be spurious, just as detrending by linear regression is known to generate spurious trends and cycles in nonstationary time series. A Monte Carlo experiment confirms that when data is generated by a random walk, the SS method tends to indicate (incorrectly) that the series consists of cyclical variations around a smooth trend. The improvement in fit over the true model will typically appear to be statistically significant. These results suggest that caution should be exercised in drawing inferences about the nature of economic processes from the SS decomposition.

Nelson, Julianne
TI Product Availability as a Strategic Variable: The Case of Retailer Stockouts. AU Katz, Barbara G.; Nelson, Julianne.

Neufeld, Wilhelm
TI Quantity Guided Price Setting. AU Dierker, Egbert; Neufeld, Wilhelm.

TI Quantity Guided Price Setting. AU Dierker, Egbert; Neufeld, Wilhelm.

Neumann, M. J. M.


AB The famous variable-slope property of the short-run Phillips-curve is not a generally valid implication of rational expectations. Instead it results from assuming that agents are restricted to observing a local market price as the only source of contemporaneous information. We show that in a more general case of a two-signals world, where agents observe a local goods price and a global asset price, changes in the variances of aggregate nominal and real stocks affect the effective output-inflation trade-off by changing the shift properties of the Phillips-curve instead of its slope. This has implications for empirical tests.

Neumark, David
PD June 1987. TI Employers' Discriminatory

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Newey, Whitney K. 

AB This paper considers adaptive estimation of regression models by means of generalized method of moment estimators. Two models are considered, that with an i.i.d. disturbance that is independent of the regressors and with a conditionally symmetric but (possibly) heteroskedastic disturbance. For both cases the paper develops linearized estimators that are asymptotically efficient if the number and variety of moment conditions is allowed to grow at an appropriate rate with the sample size. In the general symmetric case no other adaptive estimator has yet been proposed. Also, results of a small Monte Carlo study indicate that in the independence case the small sample performance of the generalized method of moments estimator can be quite good vis-a-vis other estimators previously proposed.


AB We consider the linear regression model with censored dependent variable, where the disturbance terms are restricted only to have zero conditional median (or other prespecified quantile) given the covariates and censoring point. For this model, a lower bound for the asymptotic covariance matrix for locally-regular estimators of the regression coefficients is derived. We also show how an estimator which attains this lower bound can be constructed. As a special case, our results apply to the (uncensored) linear model.

Nickell, Stephen J. 

PD This paper studies the fertility behavior underlying estimates of duration or hazard models from data on first birth intervals, in particular the meaning of the estimated effects of exogenous demographic variables on the hazard rate. Most simply, the question is whether these effects represent variation in planned or expected birth intervals, or instead direct effects on the probability of a birth. Utilization of data on timing expectations, along with the demographic variables, allows this question to be answered. The conclusion is that timing plans or expectations are the dominant empirical determinant of actual first birth durations. An implication of this, with important consequences for family policy, is that the source of high fertility among young women with certain demographic characteristics is more the result of their plans and expectations than of "mistakes" (or deviations of actual from expected timing).

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The findings that emerge are somewhat ambiguous, due to the difficulty of identifying parameters capturing all of the possible channels of influence. In one identifiable version of the model, significant family effects on labor force experience for both men and women are found, and these effects are very dissimilar by gender. In a second version, the finding on the dissimilarity of the effects is attenuated.
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AB This paper reports an attempt to discriminate between three alternative models of employment determination - labour demand, efficient bargains, and efficiency wages. Further, the importance of financial factors in employment determination is explicitly recognised. Our basic empirical result is that the firm's employment is negatively related to its own wage, and to the change in its relative wage. This is hard to rationalise within any of the three models, though it may be explicable in terms of an efficiency wage model modified to allow for the adaptation of aspirations. Our results also suggest that financial factors like income and capital gearing exert a significant effect on employment, and may be a channel through which higher inflation depresses employment.

Norman, G.
TI Price Discrimination and Equilibrium in Monopolistic Competition. AU MacLeod, W. B.; Norman, G.; Thiss, J. F.

Novales, Alfonso
TI Estimation of Dynamic Investment Functions in Oil Exploration. AU Hendricks, Ken; Novales, Alfonso.

Ordeshook, Peter

AB No discipline can claim a greater impact on contemporary political theorizing than that of economics, whether that theorizing concerns the study of legislatures, elections, international affairs, or judicial processes. This essay questions, however, whether this impact is a form of "economic imperialism," or the logical development of two disciplines whose artificial separation in the first part of this century merely allowed the development and refinement of the rational choice paradigm, unencumbered by the necessity for considering all of reality. Indeed, applications to specific substantive political matters -- most notably collective and cooperative processes where game theory proves most relevant -- reveal the paradigm's incompleteness. These applications, however, illuminate the necessary theoretical extensions, which is no longer the sole domain of the economist.

TI A Decade of Experimental Research on Spatial Models of Elections and Committees. AU McKevey, Richard; Ordeshook, Peter.

Osler, Carol L.

AB This paper considers the effect on factor prices and welfare of trade between economies whose production is characterized by nation-specific technological uncertainty. The analysis is carried out using a two-country Diamond overlapping-generations model in which technological uncertainty is reflected in factor prices, and "equities" refer to claims on the returns to capital. We find that trade in capital is complementary to trade in commodities, in the sense that adding free trade in capital to the spectrum of permitted economic activities will cause significant changes in wages, output, and capital returns. Furthermore, for countries which are identical, or not very different, factor prices move in parallel when free trade in capital is introduced. Specifically, as we show in the text, capital returns fall, while wages rise, in both countries. These results are based on the portfolio diversification permitted by international capital market integration: the reduction of portfolio risk associated with portfolio diversification induces adjustments in savings behavior which, in turn, change factor prices.


AB The paper shows that differences in real interest rates across countries can arise even with perfect competition and fully integrated international capital markets. Specifically, we find that factor returns will differ across countries which are identical except for differences in technological riskiness, overall productivity, or labor force size. We also show that differences across countries in technological riskiness, risk aversion, in population size and in overall productivity will lead to a non-zero current account in the steady state. Higher technological riskiness, greater risk aversion, and a larger population should be associated with a current account surplus. The analysis is carried out using a two-country Diamond overlapping-generations model in which technological uncertainty is reflected in factor returns.

Ouliaris, Sam
TI Asymptotic Properties of Residual Based Tests for Cointegration. AU Phillips, Peter C. B.; Ouliaris, Sam.

TI Testing for Cointegration using Principal Component Methods. AU Phillips, Peter C. B.; Ouliaris, Sam.

Owen, Guillermo
TI Paths Leadings to the Nash set. AU Maschler, Michael; Owen, Guillermo; Peleg, Berelol.

Owen, Joel
TI An Equilibrium Model of a Second Economy Market
Pagan, Adrian


AB This paper considers the estimation of a linear model containing a term representing the risk originating from a failure to perfectly predict some variable. Theoretical models show that this risk is related to the moments of the probability density function of the variable conditioned upon whatever information agents use in their optimization. The paper looks at issues arising when the level of risk is to be explained rather than when it is an explanator. Within the literature a variety of proxies for risk can be found. Section 4 looks at these to see how satisfactory each method is when used as a measure of risk in a modeling environment. In general the proxies suffer from a variant of the "errors in variables" problem, and therefore should only be used in conjunction with an instrumental variables estimator; if substituted directly into a regression an underestimate of the effect of risk on decisions is likely. An exception to this rule occurs if a parametric model for the risk term is adopted, but this methodology has its own problems involving potential misspecification, which can be partially alleviated by following our instrumental variables approach.

Parthasarathy, T.

TI Equilibria for Discounted Stochastic Games. AU Mertens, J. F.; Parthasarathy, T.

Pascal, A. H.

AB AIDS (Acquired Immune Deficiency Syndrome) ranks near the top of the list of major impairments in terms of average lifetime medical costs. A large share of the rapidly escalating costs for treating victims of the AIDS epidemic will fall on the Medicaid program. This Note reports the results of a five-month exploratory research effort that attempted to estimate these costs. The findings are only best estimates, given current knowledge. Combining assumptions as to case load, Medicaid eligibility, average treatment costs, and Medicaid reimbursement rates yields a range of estimates for cumulative Medicaid costs in 1986-1991. The intermediate estimate amounts to about $10 billion, although the most optimistic set of assumptions would yield an estimate as low as $2 billion, and the most pessimistic would produce an estimate as high as $47 billion. National total treatment costs are also estimated.

Patterson, Douglas M.
TI Linear Versus Nonlinear Macroeconomies: A Statistical Test. AU Ashley, Richard A.; Patterson, Douglas M.

Perloff, Jeffrey M.
AB This paper re-examines the effects of nominal contracts on the relationship between unanticipated inflation and individual stock's rate of return. This study differs in three main ways from previous research. First, announced inflation data are used to examine the effects of unanticipated inflation. Second, a different specification is used to obtain more efficient estimates. Third, additional nominal contracts are considered. The empirical results indicate that time-varying firm characteristics related to inflation predominate determine the effect of unanticipated inflation on a stock's rate of return. A firm's debt-equity ratio appears to be particularly important in determining the response.

Peleg, Bezalel
TI Paths Leading to the Nash set. AU Maschler, Michael; Owen, Guillermo; Peleg, Bezalel.

Perron, Pierre
AB In this paper we compare the Tobit ML estimator with a number of semi-parametric and bounded-influence estimators for the censored regression model. The comparison is carried out on the basis of an empirical example, in which we estimate Engel curves using household budget data containing a significant fraction of reported zero expenditure. The ML estimator appears to be very sensitive to extreme observations and is way off in some cases. Semi-parametric and bounded-influence estimators are close to each other and look more reliable. However, bounded-influence estimators appear to be more precise, and provide diagnostic information that is useful to identify sources of model failures.

Peristiani, Stavros
TI Bank Size, Collateral and Net Purchase Behavior in the Federal Funds Market: Empirical Evidence A Note. AU Allen, Linda; Peristiani, Stavros; Saunders, Anthony.

Perloff, Jeffrey M.

Perron, Pierre
AB This paper is a survey of the economic literature on vertical integration. It will be published by North-Holland in the Handbook of Industrial Organization, edited by Richard Schmalensee and Robert D. Willig.
Pestieau, Pierre
TI Tax-Transfer Policies and the Voluntary Provision of Public Goods. AU Boadway, Robin; Pestieau, Pierre; Wildasim, David.

Peters, Wolfgang
AB In the last decade there has been a rapidly growing interest in analysing the problems of the state pension insurance from the viewpoint of economic theory. State pension insurance increasingly has become a public issue because the usual pay-as-you-go system required excessive adjustments in both the premium and the pension structure. If such necessary adjustments were considered as politically unfeasible, financing the pension scheme could be ensured by state subsidies. Considering the far-reaching effects that any change to the pension system can have, it is clear that one of the central goals of the theoretical analysis consists in showing the relationship between the changes in the insurance system and the individual behavior of the policy-holders. For it is precisely the changing labor-leisure choice and with it the changing retirement age that substantially effect the financing of a pension system.

Peterson, Jane
TI Change in the Status of Women Across Generations in Asia. AU King, Elizabeth; Peterson, Jane; Adicioomo, Sri M.; Domingo, Lita; Syed, Sabiha H.

Phillips, Peter C. B.
AB It is shown that matrix quotients of submatrices of a spherical matrix are distributed as matrix Cauchy. This generalizes known results for scalar ratios of independent normal variates. The derivations are simple and make use of the theory of invariant measures on manifolds.

AB Examples are given to illustrate that conditional independence almost everywhere in the space of the conditioning variates does not imply unconditional independence, although it may well imply unconditional independence of certain functions of the variables. An example that is important in linear regression theory is discussed in detail. This involves orthogonal projections on random linear manifolds, which are conditionally independent but not unconditionally independent under normality.

TI Statistical Inference in Regressions with Integrated Processes: Part II. AU Park, Joon Y.; Phillips, Peter C. B.
AB This paper studies a class of models where full identification is not necessarily assumed. We term such models partially identified. It is argued that partially identified systems are of practical importance since empirical investigators frequently proceed under conditions that are best described as apparent identification. One objective of the paper is to explore the properties of conventional statistical procedures in the context of identification failure. Our analysis concentrates on two major types of partially identified model: the classic simultaneous equations model under rank condition failures; and time series spurious regressions. Both types serve to illustrate the extensions that are needed to conventional asymptotic theory if the theory is to accommodate partially identified systems. Some applications are discussed including the Gaussian AR(1) for stable, explosive and unit root coefficients.

AB Under general conditions the sample covariance matrix of a vector martingale and its differences converges weakly to the matrix stochastic integral from zero to one of BdB; where B is vector Brownian motion. For strictly stationary and ergodic sequences, rather than martingale differences, a similar result obtains. In this case, the limit is the same with a constant matrix, of bias terms whose magnitude depends on the serial correlation properties of the sequence. This note gives a simple proof of the result using martingale approximations.

AB This paper develops an asymptotic theory for
residual based tests for cointegration. These tests involve procedures that are designed to detect the presence of a unit root in the residuals of (cointegrating) regressions among the levels of economic time series. Attention is given to the augmented Dickey Fuller (ADF) test and the $Z(\alpha)$ and $Z(t)$ unit root tests recently proposed by Phillips (1987). Two new tests are also introduced, one of which is invariant to the normalization of the cointegrating regression. All of these tests are shown to be asymptotically similar and simple representations of their limiting distributions are given in terms of standard Brownian motion. The ADF and $Z(t)$ tests are asymptotically equivalent. Power properties of the tests are also studied. The analysis shows that all the tests are consistent if suitably constructed but that the ADF and $Z(t)$ tests have slower rates of divergence under cointegration than the other tests. The paper concludes by addressing the larger issue of test formulation. Some major pitfalls are discovered in procedures that are designed to test a null of cointegration (rather than no cointegration). These defects provide strong arguments against such test formulations and support the continuing use of residual based unit root tests.

Pines, D.

TI The Demand for a Risky Asset when its Returns are Stochastically Related to Prices of Consumption Goods.

AU Schwartz, A.; Pines, D.; Eldor, R.

Pines, David

PD August 1987. TI Tiebout Without Politics.

AA Department of Economics, Tel-Aviv University and the University of Western Ontario. SR Tel Aviv Foerder Institute for Economic Research Working Paper: 21-87; Department of Economics, Tel Aviv University, Ramat Aviv 69978, Tel Aviv, ISRAEL. PG 22.


AB This paper reexamines the existence and the efficiency of an equilibrium with developers who supply local public goods to maximise profits. It is shown that, as in the club theory, if communities are perfectly replicable, such an equilibrium exists and is efficient. But if communities cannot be replicated, equilibrium with profit maximizing developers need not exist, unless we adopt a strong assumption regarding the preference and the production technology. Since the assumption of perfect replicability is unrealistic in view of the uneven distribution in space of local amenities, we conclude that, in the real world, equilibrium with profit maximizing developers need not exist. Consequently, some form of political process is indispensable for efficient provision of public goods, even on a local level.

Pissarides, Christopher A.

PD November 1987. TI Unemployment and the Inter-Regional Mobility of Labour.


AB We investigate the effect of unemployment on interregional mobility in Great Britain by estimating household migration probabilities with data from the 1977 and 1984 Labour Force Surveys. We find that unemployed households are much more likely to move than employed households but regional unemployment differentials do not play an independent explanatory role in migration regressions. We also find that at higher overall unemployment rates migration probabilities are reduced everywhere both on average and at the margin.
Plott, Charles R.
TI A Study of Zero-Out Auction: Experimental Analysis of a Process of Allocating Private Rights to the Use of Public Property. AU Guler, Kemal; Plott, Charles R.; Vuong, Quang H.

Popper, Steven W.
AB In 1968, Hungary introduced a series of reforms to the central planning system. The goal was to make the economy more efficient by placing decision making authority at the level that has the most information on production and marketing possibilities – the level of the enterprise. This paper examines the situation enterprise managers face and suggests reasons that the changes in managerial behavior that were expected by the reformers, and upon which the reform is predicated, have not come easily. The author argues that reform has altered the terms of economic relations in Hungary, while the underlying structure of relations between enterprise managers and their superiors has not changed enough to allow the new system to function as intended.

Porter, David P.
TI The Design of Mechanisms to Allocate Space Station Resources. AU Banks, Jeffrey S.; Ledyard, John O.; Porter, David P.

Porter, Robert H.
TI An Empirical Study of an Auction with Asymmetric Information. AU Hendricks, Kenneth; Porter, Robert H.

Poterba, James M.
AB This paper analyzes the statistical evidence bearing on whether transitory components account for a large fraction of the variance in common stock returns. The first part treats methodological issues involved in testing for transitory return components. It demonstrates that variance ratios are among the most powerful tests for detecting mean reversion in stock prices, but that they have little power against the principal interesting alternatives to the random walk hypothesis. The second part applies variance ratio tests to market returns for the United States over the 1871-1986 period and for seventeen other countries over the 1957-1985 period, as well as to returns on individual firms over the 1926-1985 period. We find consistent evidence that stock returns are positively serially correlated over short horizons, and negatively autocorrelated over long horizons. The point estimates suggest that the transitory components in stock prices have a standard deviation of between 15 and 25 percent and account for more than half of the variance in monthly returns. The last part of the paper discusses two possible explanations for mean reversion: time varying required returns, and slowly-decaying "price fads" that cause stock prices to deviate from fundamental values for periods of several years. We conclude that explaining observed transitory components in stock prices on the basis of movements in required returns due to risk factors is likely to be difficult.

Powell, Andrew
TI The Management of Developing Country Commodity Risks: A New Role for Public Policy. AU Gilbert, Christopher; Powell, Andrew.

Powell, James L.
TI Efficient Estimation of Linear and Type I Censored Regression Models Under Conditional Quantile Restrictions. AU Newey, Whitney K.; Powell, James L.

Pulleyblank, William
TI Matroid Steiner Problems, the Tutte Polynomial and
Network Reliability. AU Colbourn, Charles J.; Pulleyblank, William R.

TI The Maximum Size of a Convex Polygon in a Restricted Set of Points in the Plane. AU Alon, N.; Katchalski, M.; Pulleyblank, W. R.

TI On Cycle Cones and Polyhedra. AU Coullard, Colette; Pulleyblank, William.

Purvis, Douglas D.

TI Taxation and Business Activity: A Survey. AU Mints, Jack M.; Purvis, Douglas D.

Putler, Daniel S.


AB This paper presents a theoretical framework to assess the effect of health information on the demand for an affected product. This framework is applied to the shell egg market. The empirical evidence suggests that health information linking diet to heart disease is responsible for reducing per capita shell egg consumption by 10 to 11 eggs per quarter (a 14 per cent reduction).


AB A method is presented to assess the effect of health information on the demand for an affected product. This method is applied to the shell egg market. Empirical evidence indicates that health information linking diet to heart disease is responsible for reducing per capita shell egg consumption by 14 per cent.


AB Despite the interest in agricultural computer use, little work has been done to examine the individual farm-firm's choice of whether or not to adopt a computer. Understanding (and quantifying) the factors that influence the farm computer adoption choice will assist interested parties in developing successful computer-oriented programs by (1) identifying their potential clientele and (2) better understanding the needs of that clientele. Consequently, the goals of this study are twofold: first, to formulate and estimate empirical models of the decision to use a computer and various types of computer applications using a theoretical choice model and discrete econometrics and, second, to identify the most likely clientele groups for both extension and agricultural education programs.

Quah, Danny


AB It is often argued that the presence of a unit root in aggregate output implies that there is no "business cycle": the economy does not return to trend following a disturbance. This paper makes this notion precise, but then develops a simple aggregative model where this relation is contradicted. In the model, output both has a unit root, and displays repeated short-run fluctuations around a deterministic trend. Some summary statistical evidence is presented that suggests the phenomena described in the paper is not without empirical basis.

Quandt, Richard E.

TI Budget Constraints, Bailouts and the Firm Under Central Planning. AU Goldfeld, Stephen M.; Quandt, Richard E.

Quinzii, M.


AB Using the Eaton and Lipsey model, we show that a hierarchical system of central places is socially optimal: firms having less frequent purchases are clustered with firms having more frequent purchases in any configuration minimizing total transport costs.


Radermacher, F. J.

TI Scheduling Project Networks with Resource Constraints and Time Windows. AU Bartusch, M.; Mohring, R. H.; Radermacher, F. J.

Ramey, Garcey

PD December 1986. TI Information Transfer and
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AB This paper considers monopoly provision of product quality for experience goods when the firm's investment in quality is distinct from its quality outcome. Thus, the problem involves moral hazard and adverse selection. In this case, the firm chooses zero investment regardless of how much information about product quality is transferred by the product's price, and even if information transfer is complete. Further, the repeat business mechanism is incapable of providing investment incentives when price is fully-informative as to quality. The market is consequently limited in its ability to provide quality, since investment in quality is incompatible with information transfer.


AB This paper analyses monopoly pricing, advertising and warranty provision when the firm and consumers are asymmetrically informed as to the quality of the product. The paper offers a general approach to the derivation of multidimensional signaling equilibria when quality can assume a continuum of possible levels. When greater actual quality has the effect of raising production costs and quality is signaled through price, the firm will choose prices above complete-information monopoly levels. Signaling through price and advertising increases consumer welfare and reduces profits relative to signaling through price alone. When quality is signaled through price and warranty, consumer welfare improves when warranties are a sufficiently close substitute for quality, and profits improve if the effect of actual quality on warranty costs outweighs its effect on production costs.

Razin, A.


AB The dynamic effects of fiscal policies on the real equilibrium have been the subject of a large body of recent research, emphasizing the intertemporal dimensions of tax and spending policies both in closed and open-economy contexts. The analysis in this paper extends the intertemporal analysis which was conducted under full certainty to uncertain environments. Specifically the paper uses a two-country stochastic general-equilibrium model of the world economy to address issues concerning the effects of government tax and spending policies on private sector consumption asset portfolios and stock market valuations. The key result of the paper is that the consequences of
expected future policies and the characteristics of their international transmission depend critically on the precise variability of these policies across states of nature. The effects of current policies on consumption savings and stock market prices are shown, however, to conform closely to the predictions of the corresponding certainty intertemporal model.


AB The dynamic effects of fiscal policies on the real equilibrium have been the subject of a large body of recent research, emphasizing the intertemporal dimensions of tax and spending policies both in closed and open-economy contexts. The analysis in this paper extends the intertemporal analysis which was conducted under full certainty to uncertain environments. Specifically the paper uses a two-country stochastic general-equilibrium model of the world economy to address issues concerning the effects of government tax and spending policies on private sector consumption asset portfolios and stock market valuations. The key result of the paper is that the consequences of expected future policies and the characteristics of their international transmission depend critically on the precise variability of these policies across states of nature. The effects of current policies on consumption savings and stock market prices are shown, however, to conform closely to the predictions of the corresponding certainty intertemporal model.

Redish, Angela
TI Credible Commitment and Exchange Rate Stability: Canada’s Interwar Experience. AU Bordo, Michael D.; Redish, Angela.

Renault, E.
TI Contraintes bilinéaires: estimation et test. AU Gourieroux, C.; Monfort, A.; Renault, E.

Reny, Philip J.

AB This paper examines an extensive form game with complete information for each player regarding previous moves. Each player chooses from an infinite action set. Such games are much more prevalent in economic applications than the finite action counterparts originally described in the literature. The contribution of the paper is to present a direct and elementary proof of the existence of subgame perfect equilibrium. It is assumed that all action sets are sequentially compact, first countable, and separable. Payoffs are continuous functions of all actions. The direct proof establishing existence also shows how finite action games can be used to approximate a given infinite-action game.

Richelle, Yves
TI Roy-Consistent Expectations. AU Allard, Marie; Bronsard, Camille; Richelle, Yves.

Richter, Marcel K.
TI Testing Strictly Concave Rationality. AU Matkin, Ross L.; Richter, Marcel K.

Robinson, Marc S.
TI Government Saving, Capital Formation and Wealth in the United States, 1947-1985. AU Boskin, Michael J.; Robinson, Marc S.; Huber, Alan M.

Robinson, Sherman

AB This paper develops an approach to analysing Jacobian multipliers that decomposes macro, sectoral, and institutional linkages in a SAM framework. The first section discusses the Jacobian multipliers and associated decomposition for a theoretical CGE model. We then discuss linkage decompositions in a SAM-based macromodel. Finally, we give an illustration of the multiplier decomposition and macro linkages with a small CGE model of the United States.

TI The Impact of Price Rigidities: A Computable General Equilibrium Analysis. AU Dewatripont, Mathias; Robinson, Sherman.

Robson, Arthur J.
TI A Simple Proof of the Existence of Subgame Perfect Equilibria in Infinite-Action Games of Perfect Information. AU Reny, Philip J.; Robson, Arthur J.

Rockett, Katharine E.
TI International Macroeconomic Policy Coordination When Policy-Makers Disagree on the Model. AU Frankel, Jeffrey A.; Rockett, Katharine E.

Rodrik, Dani

AB The ability to create appropriate incentives is often compromised by the expectation that the government will respond to future circumstances, say bailing out a dictator to avoid a bloodbath, or raising taxes on immovable capital investments. The government's dilemma, simply, is that it may be unable to commit future governments not to be responsive. Contracts and constitutional provisions are mechanisms to limit responsiveness. So too are arrangements that lower certain government payoffs to increase the cost of being responsive, or build reputations capital investments. The government's dilemma, simply, is that it may be unable to commit future governments not to be responsive. Contracts and constitutional provisions are mechanisms to limit responsiveness. So too are arrangements that lower certain government payoffs to increase the cost of being responsive, or build reputations capital investments.

AB A promising strategy for being unresponsive is to base government actions on variables not under the control of individuals, such as unalterable characteristics or aggregate outcomes. These at best are palliative measures: Informed policy makers might wish to include in the description of objects to be studied not only economic information but the names of the goods or the names of the agents. As the domain of objects (utility possibility sets, economic environments, environments with names) changes to include a thicker description of the problem, the theory changes in two ways: the axiomatic representation of the modeler's intuitions becomes more precise, but the domain axiom required to prove characterization theorems becomes increasingly strong. The conclusion is that what the modeler gains in precision is lost in credibility. This is the inherent weakness in axiomatic modelling.

Roemer, John E.


AB An international agency, such as the World Health Organization (WHO), is charged to distribute an endowment of resources among many countries, with a goal to reduce their rates of infant mortality. What allocation rule should it use? In the first part, the problem is presented abstractly, and a new axiomatic characterization of the lexicographical egalitarian allocation rule is derived. It is suggested that the axioms are ones that an international agency should endorse. In the second part, the author reports the results of his interview with WHO officials and his analysis of the WHO budget, to determine how, in fact, resources are allocated. A tension among three allocation rules is discovered: lexicographic egalitarianism, population-weighted utilitarianism, and modified country utilitarianism. The paper concludes with an evaluation of the salience of the axiomatic method as a policy guide for those who actually allocate resources.


AB Consider the problem of how to divide n resources among r agents, each of whom has specified preferences over the resources. The problem can be studied with models specifying different degrees of information. Axiomatic bargaining theory chooses to represent only the utility possibilities set and the threat point. For some purposes, this specification is too thin, and we may represent the problem by specifying the economic environment fully, that is, by postulating a domain of objects that include the preferences of the agents and the vector of goods to be divided among them. For other purposes, still more information may be requested: we might wish to include in the description of objects to be studied not only economic information but the names of the goods or the names of the agents. As the domain of objects (utility possibility sets, economic environments, environments with names) changes to include a thicker description of the problem, the theory changes in two ways: the axiomatic representation of the modeler's intuitions becomes more precise, but the domain axiom required to prove characterization theorems becomes increasingly strong. The conclusion is that what the modeler gains in precision is lost in credibility. This is the inherent weakness in axiomatic modelling.


AB While there is a quite clear picture of the rights that private ownership bestows upon the owner, it is not clear what property rights the public have by virtue of their owning a thing collectively. We ask: how should a planner, whose job is to respect public ownership of some productive assets, in conjunction with private ownership of some inputs, wish to allocate resources? We insist throughout on the desideratum that: (1) the final allocation be Pareto efficient. We propose three additional desiderata: (2) equal division of benefits derived from public ownership; (3) equal returns to the use of privately owned inputs; (4) universal gain from improvements in the publicly owned asset. No more than one of (2), (3) and (4) is in general compatible with (1). Each of the three compatible pairs of desiderata characterizes a proposal for public ownership. We call the equal benefit solution the one characterized by (1)-(2), the proportional solution the one characterized by (1)-(3) and the constant return equivalent mechanism the one characterized by (1)-(4).

Rogoff, Kenneth


AB Prior to elections, governments (at all levels) frequently undertake a consumption binge. Taxes are cut, transfers are raised, and government spending is distorted towards highly visible items. The "political business cycle" (better be thought of as "the political budget cycle") has been intensively examined, at least for the case
of national elections. A number of proposals have been
advanced for mitigating electoral cycles in fiscal policy.
The present paper is the first effort to provide a fully-
specified equilibrium framework for analyzing such
proposals. A political budget cycle arises here via a
multidimensional signalling process, in which incumbent
leaders try to convince voters that they have recently been
doing an excellent job in administering the government.
Efforts to mitigate the cycle can easily prove counterproductive, either by impeding the transmission of
information or by inducing politicians to select more costly
ways of signalling. The model also indicates new
directions for empirical research.

TI Was it Real? The Exchange Rate-Interest
Differential Relation Over the Modern Floating Rate
Period. AU Meese, Richard; Rogoff, Kenneth.

PD November 1987. TI Equilibrium Political Budget
Cycles. AA University of Wisconsin, Former National
Fellow, Hoover Institution. SR Stanford Hoover
Institute Working Paper in Economics: E-87-48; Domestic
Studies Program Working Paper Series, Hoover
Institution, Stanford University, Stanford, CA 94305.
PG 49. PR No Charge. JE 321, 322, 131, 023.
Elections.

AB Prior to election, governments (at all levels)
frequently undertake a consumption binge. Taxes are cut,
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information or by inducing politicians to select more costly
ways of signalling. The model also indicates new
directions for empirical research.

Romer, Christina D.
PD November 1987. TI Changes in the Cyclical
Behavior of Individual Production Series. AA National
Bureau of Economic Research. SR National Bureau of
of Economic Research, 1050 Massachusetts Avenue,
Cambridge, MA 02138. PR $2.00. JE 042, 131, 111.

AB This paper uses simple time series techniques to
analyze changes in the short-run behavior of 38 physical
production series for 1889-1984. The main finding is that
fluctuations in these output series in the periods 1889-1914
and 1947-1984 are very similar, while those in the period
1922-1959 are anomalous. Relative to the prewar era, the
postwar era exhibits only a slight damping of fluctuations
and no increase in the persistence of short-run movements.
At the same time, the correlation between the growth rates
of the 38 goods is very low in both the prewar and postwar
eras and has declined slightly over time.

Romer, David
TI The Equilibrium and Optimal Timing of Price
Changes. AU Ball, Laurence; Romer, David.

Rose, Nancy L.
TI The Effects of Economic Regulation. AU Joskow,
Paul L.; Rose, Nancy L.

Rosen, Harvey S.
TI Federal Deductibility and Local Property Tax Rates.
AU Holts, Eakin Douglas; Rosen, Harvey S.

Rosen, Sherwin
PD May 1987. TI Transactions Costs and Internal
Labor Markets. AA University of Chicago.
SR Economics Research Center/NORC Discussion
Paper: 87-12; Economics Research Center/NORC, 6030
South Ellis, Chicago, IL 60637. PG 26. PR $2.00;
send requests to Librarian, NORC. JE 821, 851, 512,
022. KW Agency Theory. Personnel Management

AB The concept of transactions costs used by Coase in
"The Nature of the Firm" is applied to the internal labor
market of an organization. Under joint production it is
shown that the number of transaction-specific prices
necessary to decentralize labor allocations rises
geometrically with the size of the work force. Complexity
of calculation and costs of implementation constrains the
possibilities for internal decentralization through a price
mechanism and substitutes a more authoritarian system of
allocation instead. These same issues of complexity and implementation costs limit the usefulness of agency theory as a conceptual framework for this problem. The analysis suggests that an internal labor market must be viewed in a more comprehensive framework of a personnel management system.


AB The market equilibrium consequences of optimal herd-inventory management are worked out for farm animal populations. A permanent change in demand implies backward-bending short-run and elastic long-run supply responses, but transitory changes imply the usual rising supply price response. Furthermore, increasing inventories are associated with high and falling prices and conversely for decreasing inventories, but there is no market instability in this. These unusual intertemporal substitution effects follow from both rational expectations and appropriately formulated cobweb theories and go part way toward explaining the market cyclical patterns observed in hog and cattle inventories. Forthcoming in the American Journal of Agricultural Economics.


AB A valuation formula is derived for changes in age-specific mortality risks using life-cycle expected utility theory. These methods are useful for valuing activities involving substantial delays between exposure and risk, such as consumption of carcinogens, and for cost-benefit analysis of medical research. The methodology implies straightforward connections between cross-section value-of-life estimates and the appropriate life-cycle estimates. Illustrative calculations are presented based on one cross-section study of equalizing differences in wage-rates. Issues of randomization, time-consistency in valuations, regret for past actions and how valuations change over the life-cycle are also discussed.

Ross, Thomas W.


AB This paper studies the response of a dominant domestic oligopoly to the reduction in the rate of a protective tariff. The issue here is whether domestic market performance is improved through a movement toward free trade alone. Put another way, is free trade always a substitute for competition policy? We find that the lower tariff may lead to inferior domestic market performance. The direction of the change and its magnitude are functions of the shape of the import supply function, the degree of competition between oligopolists and whether or not entry is possible. Thus, there is reason to believe that a strong competition policy may, in some markets be complementary to free trade.

TI Warranties Without Commitment to Market Participation. AU Bigelow, John; Cooper, Russell; Ross, Thomas W.

Roubini, Nouriel

ABSTRACTS


AB This paper uses a global macroeconomic simulation model to identify the factors that have contributed to global trade and financial imbalances in the 1980s. After investigating the properties of monetary and fiscal policies in the model, we examine whether the budgetary shifts in the OECD economies in the 1980s can account for the bulk of trade and exchange rate movements. Our conclusions are mixed. The combination of sharply higher fiscal deficits in the United States and sharply reduced deficits in Japan goes far to explain the movements of the trade balances and exchange rates of the two economies. However, the drop in the dollar vis-a-vis the Yen since late 1985 is not well explained by the model. We also investigate the prospects for a reduction of the United States trade deficits if United States budget deficits are in fact reduced, as well as the possible role for Japanese monetary and fiscal policies in reducing the trade imbalances of the two countries.

Rubinstein, Ariel

AB It is pointed out that the outcome of decentralized trading is not necessarily Walrasian even when the market is frictionless. The equilibria that support non-Walrasian outcomes are interpreted as corresponding to markets in which the institutional structure is such that the interaction between agents depends on their identities and is affected by personal relationships that may develop between them. It is shown that, in frictionless markets in which the interaction between agents depends only on impersonal market information, the unique outcome of decentralized trading is the Walrasian outcome.

Ruttan, Vernon W.
TI Development Policy under Eisenhower and Kennedy. AU Hagen, James M.; Ruttan, Vernon W.

Sachs, Jeffrey
TI Sources of Macroeconomic Imbalance in the World Economy: A Simulation Approach. AU Roubini, Nouriel; Sachs, Jeffrey.

Sadoulet, Elisabeth
TI Agrarian Structure, Technological Innovations, and the State. AU de Janvry, Alain; Sadoulet, Elisabeth; Falchamps, Marcel.

TI Agricultural Growth and Import Demand in the LDCs. AU de Janvry, Alain; Sadoulet, Elisabeth.

TI Investment Strategies to Combat Rural Poverty: A Proposal for Latin America. AU de Janvry, Alain; Sadoulet, Elisabeth.

Safra, Zvi

AB Consider a feasible set, X, of C.D.F.'s. Assume that the set of decision makers, who must choose from X, includes non-expected utility decision makers who are risk averse in some weaker notions. We show that in this case the efficient set of X expands relative to the expected utility case. We characterize the efficient sets for each notion of risk aversion including the expected utility case. It is also shown that the limited-coverage insurance policies, which are not efficient under the expected utility hypothesis, belong to the efficient set when weakly risk averse non-expected utility functional are assumed to exist.

TI Ascending Bid Auctions with Behaviorally Consistent Bidders. AU Karni, Edi; Safr, Zvi.

Salant, Stephen

AB Stokey (1979) showed in an intertemporal context that, under reasonable assumptions, price discrimination is never optimal if a monopolist can pre-commit to a price path. This note explores the implications of Stokey's result for the optimality of inducing self-selection in the static quantity and quality contexts of Spence (1980) and Mussa-Rosen (1978). It is shown that Stokey's result carries over to these other contexts under appropriate curvature assumptions. Moreover, even under traditional curvature assumptions, inducing self-selection may be suboptimal. Necessary and sufficient conditions for discrimination to be optimal are derived for the two-type case.


AB This paper reports on four series of experiments in a
five-person committee voting under majority rule. Each of two voting procedures was paired with each of two types of preference sets. The types were characterized as high or low intensity. Every set of preferences had a Condorcet point and that point was the best alternative for one (and only one) voter. When the high intensity preferences were used, committees operating under either voting procedure selected the Condorcet point more than 90 per cent of the time; when low intensity payoffs were used, the success rate was less than 51 per cent. A theory is suggested which predicts which preference sets should successfully induce selection of the Condorcet point and which should not; in the latter case, the same theory predicts that the choice will be confined to a certain collection of the other points. Our observations are consistent with this theory.


AB There are two ways to calculate the dynamic path of aggregate extraction when there is free access to a common property resource: (1) calculate the rent-dissipating aggregate extraction in any period (as a function of the stock) and then derive the dynamic path using the transition equation and initial condition or (2) examine the path of aggregate extraction in a subgame perfect equilibrium as the number of players expands without bound. The latter approach is theoretically correct but often intractable. The former approach, which has been widely used for more than thirty years, is tractable and generally presumed to yield the identical aggregate extraction path. We show by example that this presumption is erroneous. We then provide conditions which suffice for the traditional approach to be correct.


AB The report is divided into two parts. In part one, we provide an overview of attrition at the Air Force Academy, then summarize several widely accepted findings of the attrition literature which have influenced our modeling, then describe our model's structure, and then turn to illustrative simulations of the effects of policy changes. Two types of policy changes are illustrated: 1) selection policies which alter the composition of the entering class but not student incentives and 2) environmental policies which alter cadet (and applicant) incentives. Part one concludes with a discussion of how the model can be estimated. Part two, which is self-contained, describes the main program and the six subroutines which comprise the computerized implementation of the model. The report contains two appendices. The appendix to part one is a historical summary of the service obligations faced by dropouts from the Class of 1959 onwards. The appendix to part two is a listing of the computer program.


AB Although Block, Nold and Sidak sought to build in part on the prior work of Breit and Elzinga, they neglected to incorporate the central insight of Breit and Elzinga that the prospect of treble damages stimulates demand at any given price. Breit and Elzinga in turn failed to note that in anticipation of this outward shift in demand, colluding sellers will adjust their price. The purpose here is to take account both of the incentive of the buyers to "get damaged" and its effect on the pricing strategy of the sellers. Under a plausible condition on the exogenous data, a neutrality result is shown to hold. Under this condition, imposition of a multiple-damage regime has no effect on output, aggregate surplus or its expected distribution relative to laissez-faire and must raise the market price. When this neutrality result does not hold, imposing multiple damages increases output and aggregate surplus while reducing the expected surplus of the sellers. We begin by characterizing the market equilibrium in the absence of any antitrust enforcement. We then reconsider Block, Nold and Sidak's assessment of the multiple-damage regime -- taking proper account of the buyers' "perverse incentives." The conditions when the neutrality result holds are characterised and comparative statics results are derived with and without neutrality.

Saloner, Garth
TI Coordination Through Committees and Markets. AU Farrell, Joseph; Saloner, Garth.

Sappington, David
TI Regulating a Monopolist with Unknown Demand and Cost Functions. AU Lewis, Tracy R.; Sappington, David E. M.

TI Regulating a Monopolist with Unknown Demand. AU Lewis, Tracy R.; Sappington, David E. M.

TI Sharing Productive Knowledge in Internally Financed R&D Contests. AU Bhattacharya, Sudipto; Glazer, Jacob; Sappington, David E. M.

TI Countervailing Incentives in Agency Problems. AU Lewis, Tracy; Sappington, David E. M.

TI Motivating Exchange of Knowledge in R&D Ventures: First-Best Implementation. AU Bhattacharya, Sudipto; Glazer, Jacob; Sappington, David.

TI Capital Grants and Inflexible Rules in Incentive Problems. AU Lewis, Tracy R.; Sappington, David E. M.

TI Capital Grants and Inflexible Rules in Incentive Problems. AU Lewis, Tracy R.; Sappington, David.
Saunders, Anthony
TI Bank Size, Collateral and Net Purchase Behavior in the Federal Funds Market: Empirical Evidence A Note. AU Allen, Linda; Peristiani, Stavros; Saunders, Anthony.

Schankerman, Mark
TI The Interaction Between Capital Investment and R&D in Science-Based Firms. AU Lach, Saul; Schankerman, Mark.

Scharfstein, David
TI Simultaneous Signaling to the Capital and Product Markets. AU Gertner, Robert; Gibbons, Robert; Scharfstein, David.

Scheffman, David T.

AB This paper develops an analysis of markets in which sellers have significant sunk investments; it takes considerable time to enter; and buyers can make credible commitments to obtain alternative sources of supply. We show that in markets with these characteristics the market power of sellers is more attenuated than models with unsophisticated buyers would predict. In particular, current prices are critical to the decision whether or not to "enter," so that limit pricing is a likely form of equilibrium pricing, even in the presence of full information. The limit price is predicted to increase with the amount of time it takes to enter, the number of buyers, and with the level of buyers' switching costs, but to fall with the level of sunk investments. Thus, in such markets, sunk costs restrain, rather than increase, the ability of sellers to exert market power, and hence do not constitute entry barriers. Entry lags and switching costs, however, do enhance the ability of sellers to exert market power. This paper, then, questions the standard prediction of an inverse relationship between market performance and sunk investments.

Schmeidler, David
TI Information Dependent Games: Can Common Sense be Common Knowledge? AU Gilboa, Itzhak; Schmeidler, David.

Schmidt, Peter
PD November 1987. TI Models for which the MLE and the Conditional MLE Coincide. AU Cornwell, Christopher; Schmidt, Peter.


AB In this paper we develop a survival time model in which the probability of eventual failure is less than one, and in which both the probability of eventual failure and the timing of failure depend (separately) on individual characteristics. We apply this model to data on the timing of return to prison for a sample of prison releasees, and we use it to make predictions of whether or not individuals return to prison. Our predictions are more accurate than previous predictions of criminal recidivism. The model we develop has potential applications in economics; for example, it could be used to model the probability of default and the timing of default on loans.

Schrijver, A.
TI Chvatal Closures for Mixed Integer Programming Problems. AU Cook, W.; Kannan, R.; Schrijver, A.

Schwartz, A.
TI The ECU--An Imaginary or Embryonic Form of Money: What Can We Learn from History? AU Bordo, Michael D.; Schwartz, Anna J.

PD November 1987. TI The Demand for a Risky Asset when its Returns are Stochastically Related to Prices of Consumption Goods. AU Schwartz, A.; Pines, D.; Eldor, R. AA Schwartz and Pines: Department of Economics, Tel Aviv University. Eldor: Department of Economics, Boston University. SR Tel Aviv Foerder Institute for Economic Research Working Papers: 30-87; Department of Economics, Tel Aviv University, Ramat Aviv 69978, Tel Aviv, ISRAEL. PG 50. PR No Charge. JE 022, 024. KW Portfolio Selection.
AB The presence of a stochastic relation between the returns on a risky asset and a price of a consumption good alters the effects of parametric changes on the demand for a risky asset and on the expected utility of a consumer-investor from what they are in the classical case in which such a relation does not exist. In particular the qualitative equivalence of the effects of risk and risk aversion on the demand for a risky asset breaks. The reason for this departure from the classical portfolio selection behavior is the existence of conflicting objectives. On the one hand the consumer-investor prefers a stable income over a random income with the same expected value. On the other, he prefers a lottery in the price of a consumption good over an assured price which equals the expected value of the lottery. These conflicting objectives come into play if the consumer-investor's income is stochastically related to a price of a consumption good. This is the case if the rate of return on the risky asset is stochastically related to a price of a consumption good.

Shapiro, Carl
TI Dynamic Competition with Switching Costs.
AU Farrell, Joseph; Shapiro, Carl.

Sharkey, W. W.
AB The objective of this paper is to examine the nature of competition in a deregulated telecommunications network. When firms on separate links myopically set prices for a jointly provided service the Nash equilibrium is inefficient. When firms in two separate markets directly compete there may be no pure strategy equilibrium if there is a fixed cost of production or a cost advantage for each firm in its home market. In this paper the mixed strategy equilibria are computed and their properties commented upon.

Sheshinski, Eytan
AB We analyze the optimum consumption path of an individual who maximizes expected discounted utility over an infinite horizon, when savings earn a fixed return and wage earnings follow a two-state random process. It is assumed that no insurance is available against earnings uncertainty. We show that optimum consumption always changes discontinuously with the level of earnings. The optimum consumption path is characterized for the case where the subjective discount rate is equal to the interest rate. While under certainty consumption is constant in this case, it is shown that here consumption strictly increases or decreases over time. Specifically, when the 'Hazard-Rate' non-decreases with time, consumption approaches infinity or zero, respectively. The discontinuity in consumption, however, is always smaller than the difference in earnings across states. Comparison to the full insurance case when earnings can be annuitized is also provided.

Shiller, Robert J.
AB This paper consolidates and interprets the literature on the term structure, as it stands today. Definitions of rates of return, forward rates and holding returns for all time intervals are treated here in a uniform manner and their interrelations, exact or approximate, delineated. The concept of duration is used throughout to simplify mathematical expressions. Continuous compounding is used where possible, to avoid arbitrary distinctions based on compounding assumptions. Both the theoretical and the empirical literature are treated. The attached tables by J. Huston McCulloch give term structure data for United States government securities 1946-1987. The tables give discount bond yields, forward rates and par bond yields as defined in the paper. The data relate to the concepts in the paper more precisely than does any previously published data series.
TI Prices of Single Family Homes Since 1970. New Indexes for Four Cities. AU Case, Karl E.; Shiller, Robert J.
AB Questionnaires were sent out at the time of the October 19, 1987 stock market crash to both individual and institutional investors inquiring about their behavior during the crash. Nearly 1000 responses were received. The survey results show that: 1. No news story or rumor appearing on the 19th or over the preceding weekend was responsible for investor behavior, 2. Investors' importance rating of news appearing over the preceding week showed only a slight relation to decisions to buy or sell, 3. There was a great deal of investor talk and anxiety around October 19, much more than suggested by the volume of trade, 4. Many investors thought that they could predict...
the market. Both buyers and sellers generally thought before the crash that the market was overvalued. Most investors interpreted the crash as due to the psychology of other investors. Many investors were influenced by technical analysis considerations. Portfolio insurance is only a small part of predetermined stop-loss behavior, and some investors changed their investment strategy before the crash.

Shleifer, Andrei
AB The paper questions the common view that share price increases of firms involved in hostile takeovers measure efficiency gains from acquisitions. Even if such gains exist, most of the increase in the combined value of the target and the acquirer is likely to come from stakeholder wealth losses, such as declines in value of subcontractors' firm-specific capital or employees' human capital. The use of event studies to gauge wealth creation in takeovers is unjustified. The paper also suggests a theory of managerial behavior, in which hiring and entranching trustworthy managers enables shareholders to commit to upholding implicit contracts with stakeholders. Hostile takeovers are an innovation allowing shareholders to renge on such contracts, as long as managers will. On this view, shareholder gains are redistributions from stakeholders, and can in the long run result in deterioration of trust necessary for the functioning of the corporation.

Shughrat, II Wm
TI Price Leadership with Incomplete Information. AU Higgins, Richard; Shughrat, II Wm; Tollison, Robert.

Sibley, D. S.
TI An Analysis of Tapered Access Charges for End Users. AU Heyman, D. P.; Lazorchak, J. M.; Sibley, D. S.; Taylor, W. E.

Sichel, Daniel E.
AB This paper defines two types of asymmetry in business cycles: steepness and deepness. Steepness refers to cycles in which the slope of contractions exceeds the slope of expansions. Deepness refers to cycles in which troughs are further below trend than peaks are above. Previous research has focused exclusively on steepness. Two tests for deepness are proposed and applied to United States Postwar quarterly unemployment, real GNP, and industrial production. Statistically significant evidence of deepness is found for all three variables. Monte Carlo power simulations indicate that this finding is consistent with either a random walk with drift or a linear deterministic trend.

Silvestre, Joaquim

Simon, Leo K.
PD July 1987. TI Exclusive Form Games in Continuous Time: Pure Strategies. AU Simon, Leo K.; Stinchcombe, Maxwell B. AA Simon: Department of Economics, University of California at Berkeley. Stinchcombe: Department of Economics, University of California at San Diego. SR University of California at Berkeley Working Paper in Economics: 8748; IBER, 156 Barrows Hall, University of California, Berkeley, CA 94720. PG 57. PR $3.50. JE 026, 611, 022. KW Game Theory. Continuous-Time Games. Subgame Perfect Equilibrium. Coordination Games. Patent Races. AB We propose a new framework for modelling games in continuous time. Continuous time is viewed as "discrete-time, but with a grid that is infinitely fine." We apply the model to several standard problems from the industrial organization literature. We then address questions such as: "Is discrete time with a very fine grid a good proxy for continuous time?" and "does every continuous-time equilibrium in our model have a discrete-time analog?"

PD July 1987. TI Basic Timing Games. AA Department of Economics, University at Berkeley. SR University of California at Berkeley Working Paper in Economics: 8745; IBER, 156 Barrows Hall, University of California, Berkeley, Berkeley, CA 94720. PG 56. PR $3.50. JE 026. KW Game Theory. Continuous Time Games. Subgame Perfect Equilibrium. Behavior Strategies. Noisy Duel. Cournot. Stackelberg. Discrete Time Games. AB We propose a new approach to modelling finite-move, closed-loop games in continuous time. Continuous time is modeled as "discrete-time, but with a grid that is arbitrarily fine." We construct a "calculus for continuous-time games" that enables us to solve a certain class of timing games with a minimum of computation. Our machinery yields sharp and intuitive results for a range of interesting economic problems. These problems include games that might be hard to solve in discrete time without a great deal of computation. The paper concludes with an example of a continuous-time game with a subgame perfect equilibrium that is far away from any approximate equilibrium of any nearby discrete-time game.

Smith, Gregor W.

AB Deviations from ergodicity in fundamentals may give rise to apparent bubbles (non-stationary residuals) in time series models of asset prices if an econometrician is unaware of them. This paper examines a number of such deviations in the form of expected, future, regime changes and explicitly calculates the effects of this misspecification. Some positive theories of currency reform and exchange rate pegging with endogenous process switching do not generally give rise to apparent bubbles.


AB Macroeconomic theories in which there is a fixed cost to changing prices have proliferated recently. This paper solves a menu-cost pricing problem faced by a monopolistic firm in continuous time and subject to both the stochastic aggregate price level emphasized by Sheshinski and Weiss (1983) and the stochastic demand and cost disturbances emphasized by Barro (1972). It finds closed-form expressions for the time-varying trigger points of an optimal pricing strategy. These controls are forward-looking since the economy is not assumed to be in a steady state. The analysis suggests some guidelines for microeconomic tests of the menu-cost pricing hypothesis. It also provides an example of how conditional heteroskedasticity can arise endogenously in an optimizing model.


AB This paper investigates whether public financial policy satisfies a borrowing constraint. Direct tests of the present-value relation suggested by this constraint are rare, despite widespread discussion of the feasibility of current policy. We examine monthly data on Canadian federal government finances using tests for cointegration. We also conduct variance bounds tests of the present-value relation between debt and surpluses. The results indicate that although real debt and real surpluses are nonstationary processes, their joint behaviour is consistent with a government borrowing constraint. Also the variability in current debt can be accounted for by the variability in anticipated future surpluses.

TI Calibration as Estimation. AU Gregory, Allan W.; Smith, Gregor W.

Smith, Vernon L.


AB Laboratory experimentation changes the way you think about economics. Theory and observation become co-equal complimentary means for deepening our operating knowledge of how economic processes work. "Better" theory, that increases empirical content and narrows the distance between observation and prediction, is always in order whether or not the implications of current theory fail some particular null hypothesis test. At best such tests merely yield some measure of the urgency of the demand for better theory. The naive falsificationist view of "science" does not and should not characterise our intellectual task. As indicated by the quotation from Weinberg, the dialogue between observation and theory development will sometimes yield lags in either empirical research or in theory. Unfortunately, in economics, the lag in theory tends to be endemic. In addition to gaps between theory and observation, there are gaps between different sets of experimental observations, that need to be filled. An example of the latter is the discrepancy between the observations of a psychologist on how subjects think about economic problems, and observations on how subjects actually behave in the context of many experimental markets. It appears that subject behavior based upon "thinking about it" is often modified when such behavior fails to be sustained by market equilibrating forces. We also discuss the relation between experimental methods and institutional design.

Sopher, Barry

TI An Experimental Analysis of Bargaining and Strikes with One-sided Private Information. AU Forsythe, Robert; Kennan, John; Sopher, Barry.

Spear, Stephen


Spiller, Pablo T.

TI Buyers and Entry Barriers. AU Scheffman, David T.; Spiller, Pablo T.

TI Buyers and Entry Barriers. AU Scheffman, David T.; Spiller, Pablo T.

Srivastava, Sanjay


Stark, Oded

TI Consumption Smoothing, Migration and Marriage: Evidence from Rural India. AU Rosenzweig, Mark R.; Stark, Oded.
Steinmeier, Thomas L.
TI Pensions, Efficiency Wages and Job Mobility.
AU Gustman, Alan J.; Steinmeier, Thomas L.

Stinchcombe, Maxwell B.
TI Exclusive Form Games in Continuous Time: Pure Strategies.
AU Simon, Leo K.; Stinchcombe, Maxwell B.

Stock, James H.
KW Unit Roots. Integration. Consumption. Permanent Income Hypothesis.
AB We use recent research on estimation and testing in the presence of unit roots to argue that Hall's (1978) t and F tests of whether consumption is predicted by lagged income, or by lags of consumption beyond the first, are asymptotically valid. A Monte Carlo experiment suggests that the asymptotic t and F distributions provide a good approximation to the actual finite sample distribution.

Stockman, Alan C.
KW Exchange Rate. Policy.
AB The equilibrium approach to exchange rates shows that exogenous disturbances to preferences, technology, or certain government policies can change the nominal and real exchange rates in ways that are consistent with the evidence. Specifically, changes in nominal and real exchange rates are highly correlated, the exchange rates may be approximately random walks, and there are no simple relations between exchange rates and the current account. The interpretations of evidence on exchange rates and the policy conclusions that emerge from this set of models differ from the standard ones.

Summers, Lawrence
TI Mean Reversion in Stock Prices: Evidence and Implications. AU Poterba, James M.; Summers, Lawrence H.

TI Employee Crime, Monitoring and the Efficiency Wage Hypothesis. AU Dickens, William T.; Katz, Lawrence; Lang, Kevin; Summers, Lawrence.
TI Mean Reversion in Stock Prices: Evidence and Implications. AU Poterba, James M.; Summers, Lawrence H.
TI Breach of Trust in Hostile Takeovers. AU Shleifer, Andrei; Summers, Lawrence H.

Swamy, P. A. V. B.
AB In recent years, the Australian financial system has been almost completely deregulated. Financial deregulation has integrated Australia much more firmly into the international financial network and paved the way for the improved functioning of financial markets within Australia. Yet it has also introduced complications in interpreting the behavior of the monetary aggregates, as evidenced by an unexpectedly large surge in the quantity of money in late 1984 and in 1985, and led to the abandonment of monetary targeting. This study examines the factors underlying the move toward the deregulation of the Australian financial market and analyzes the changed nature of monetary policy in the deregulated environment. A main focus of the paper is on money-demand predictability. Empirical results are presented which show that random-coefficient estimation of money-demand models that incorporate inflationary expectations not only greatly reduces forecast errors, but eliminates any tendency to underpredict real money balances in late 1984 and 1985.

TI Finite Sample Properties of Theil's Measure of Multicollinearity Effect. AU Mehta, J. S.; Swamy, P. A. V. B.

Syed, Sabiha H.
TI Change in the Status of Women Across Generations in Asia. AU King, Elizabeth; Peterson, Jane; Adicotomo, Sri M.; Domingo, Lita; Syed, Sabiha H.

Tavlas, George S.
TI Financial Deregulation, the Demand for Money, and Monetary Policy in Australia. AU Swamy, P. A. V. B.; Tavlas, George S.

Taylor, J. Edward

Taylor, W. E.
TI An Analysis of Tapered Access Charges for End Users. AU Heyman, D. P.; Lazorchak, J. M.; Sibley, D. S.; Taylor, W. E.

Tesfatsion, Leigh
TI A Fortran Program for Time-Varying Linear Regression Via Flexible Least Squares. AU Kalaba, Robert; Rasakhoo, Nima; Tesfatsion, Leigh.

Thissine, Jacques Francois
TI Spatial Price Policies and Duopoly. AU Anderson, Simon P.; DePalma, Andre; Thissine, Jacques Francois.

TI On the Optimality of Central Places. AU Quinii, Martine; Thissine, Jacques Francois.
TI Price Discrimination and Equilibrium in
Prices change between the input dates and the sale date. Services and intermediate goods at various previous dates. Depreciation.

The accounting definition used in taxing profits can have movements create ambiguities in the reckoning of profits. Especially in periods of general inflation, these price analogies effects on after-tax returns from fixed capital.

Sales today were made possible by inputs of factor services and intermediate goods at various previous dates. Prices change between the input dates and the sale date. Especially in periods of general inflation, these price movements create ambiguities in the reckoning of profits. The accounting definition used in taxing profits can have significant economic effects. Tax accounting is generally not neutral vis-a-vis general inflation. Costing inputs at their historical nominal prices (FIFO) is a real burden and disincentive, greater the higher the inflation rate. It is analogous to depreciating durable capital at historical cost. However, it may be partially, completely, or excessively offset by another non-neutrality, the deductibility of nominal interest from taxable income. This too has analogous effects on after-tax returns from fixed capital.

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sustained regardless of aid from the outside; when aid is not available, dependence on domestic resources has sufficed, as illustrated by Syria. 4) Foreign aid, however, is most significant in facilitating credit and allowing the sale of arms to the three countries. 5) Military expenditure has had no positive effect on the economic structure in any of the three countries, as shown by the prevailing economic structure and the composition of the foreign trade basket. Where some impact may have taken place it is where the technology has been advanced enough to absorb and domestic the techniques brought in by military expenditure.

Ullah, Aman


AB In this paper we have reviewed and explored the nonparametric density estimation approach for analyzing various econometric functionals. The applications of density estimation have been emphasized in the specification, estimation, and testing problems arising in econometrics. Some limitations of the nonparametric approach are also examined, and potential future areas of applied and theoretical research have been indicated.


TI The Econometric Analysis of Models with Risk Terms. AU Pagan, Adrian; Ullah, Aman.

Usher, Dan


AB From the Wealth of Nations to the present day, there has been a great cycle of opinion about the sources of inefficiency, from Smith's sharp and unqualified contrast between private sector enterprise and public sector sloth, to Mill's qualified and reluctant allowance of large domains within the economy where the public sector must act because the private sector would not or could not do so, to Sidgwick's concern in the latter part of the nineteenth century with what we would now call market failure and his willingness to trust the public sector to put things right, to Pigou's detailed analysis in the early years of the twentieth century of the defects of the competitive economy coupled with an almost complete disregard of the possibility of public sector inefficiency, to a recent revival of interest in public sector economics and a reassessment of public sector efficiency reminiscent of the views of Adam Smith.


AB Intensity of preference would be irrelevant to the outcome of public decision-making by majority-rule voting if each issue were resolved in a separate plebiscite. It is not irrelevant when issues are combined in platforms of political parties. Intensity of preference can be represented as a parameter in the voter's utility function. Occasions may arise when a minority of a given size gets its way if and only if its intensity parameter is high. Minorities may also prevail over majorities by organizing to act as though their preferences were intense.

van Damme, Eric


AB This note describes an example of a repeated game which has a unique renegotiation-proof equilibrium (Farrell (1983)) that however is not stable in the sense of Kohlberg and Mertens (1986). Hence, the requirements of renegotiation-proofness and stability may be mutually inconsistent.

van der Ploeg, C. E.


AB This paper presents an alternative to models of unemployment where firms and unions negotiate over wages. Apart from wage formation the basic structure of the model is standard: monopolistic competition in an open economy, estimated on aggregate, quarterly United Kingdom data. However the assumption that firms set wages unilaterally according to the efficiency wage hypothesis yields two original features in the empirical model: (i) an efficiency variable which estimates labour productivity as a function of unemployment and supply-side variables and which identifies the price equation, and (ii) supply-side policy has a non-linear effect on unemployment, its effect decreasing as unemployment increases. The rise in productivity and profits since the
early 1980's and continuing increases in both wages and unemployment are empirical facts that cannot be explained satisfactorily within a bargaining framework, yet are not inconsistent with the efficiency wage model.

van der Ploeg, Frederick
PD November 1987. TI International Interdependence and Policy Coordination in Economics with Real and Nominal Wage Rigidity. AA Centre for Labour Economics, London School of Economics. SR London School of Economics Centre for Labour Economics Discussion Paper: 294; Centre for Labour Economics, London School of Economics, Houghton Street, London WC2A 2AE, United Kingdom. PG 70. PR No Charge. JE 451, 311, 321, 411. KW International Interdependence. Locomotive Policy. Beggars-thy-neighbor Policy. OECD Economies. Monetary Policy. Fiscal Policy. AB The development of the seven main OECD economies during the seventies and eighties is discussed. Subsequently, wage equations of the error-correction type for the seven largest OECD economies are estimated. The hypothesis of real wage rigidity cannot be rejected for the French, German, Italian and Japanese economies, but the Canadian, United Kingdom and United States economies display a significant degree of nominal wage rigidity. An analytical two-country model with floating exchange rates, uncovered interest parity, imperfect substitution between home and foreign goods, and sluggish labour markets is then formulated.

van Wijnbergen, Sweder
TI Tariffs, the Real Exchange Rate and the Terms of Trade: On Two Popular Propositions in International Economics. AU Edwards, Sebastian; van Wijnbergen, Sweder. AB The development of the seven main OECD economies during the seventies and eighties is discussed. Subsequently, wage equations of the error-correction type for the seven largest OECD economies are estimated. The hypothesis of real wage rigidity cannot be rejected for the French, German, Italian and Japanese economies, but the Canadian, United Kingdom and United States economies display a significant degree of nominal wage rigidity. An analytical two-country model with floating exchange rates, uncovered interest parity, imperfect substitution between home and foreign goods, and sluggish labour markets is then formulated.

Varian, Hal R.
PD January 1987. TI Differences of Opinion in Financial Markets. AA University of Michigan. SR University of Michigan Center for Research on Economic and Social Theory Working Paper: 87-23; Department of Economics, University of Michigan, Ann Arbor, MI 48109. PG 28. PR No Charge. JE 022, 318. KW Asset Prices. Trade Generation. Differences in Beliefs. AB Agents trade because of differences in endowments, tastes and beliefs. In the standard models of finance beliefs are assumed to be identical across agents so that trade is due only to differences in endowments and tastes. In this paper I investigate trade due to different beliefs. Differences in equilibrium beliefs may be due to different opinions (i.e., prior probabilities) or different information (i.e., different values of the likelihood function). Using modified versions of a mean-variance model due to Grossman and an Arrow-Debreu model due to Milgrom-Stickley I argue that differences in information will not in general cause trade. Rather it is only differences in opinion that generate stock market volume. I then go on to examine the effect of different opinions on asset prices. I show that if tastes are identical, and if risk tolerance does not grow too rapidly, then assets that have more dispersed opinions will, other things being equal, have lower prices and a greater volume of trade. In general the effect of differences of opinion on asset prices will depend on the curvature of asset demand functions with respect to the opinions of the agents.

TI Taxation of Asset Income in the Presence of a World Securities Market. AU Gordon, Roger H.; Varian, Hal R.
PD July 1987. TI Price Discrimination. AA University of Michigan. SR University of Michigan Center for Research on Economic and Social Theory Working Paper: 87-26; Department of Economics, University of Michigan, Ann Arbor, MI 48109. PG 55. PR No Charge. JE 022, 024. KW Monopoly. Welfare Costs. AB Price discrimination is one of the most prevalent forms of marketing practices. One may occasionally doubt whether firms really engage in some of the kinds of sophisticated strategic reasoning economists are fond of examining, but there can be no doubt that firms are well aware of the benefits of price discrimination. Three conditions are necessary in order for price discrimination to be a viable solution to a firm's pricing problem. First, the firm must have some market power. Second, the firm must have the ability to sort consumers. And third, the firm must be able to prevent resale. We will briefly discuss each of these points, and develop them in much greater detail in the course of the paper.

PD August 1987. TI Optimal Tariffs and Financial Assets. AA University of Michigan. SR University of Michigan Center for Research on Economic and Social Theory Working Paper: 87-29; Department of Economics, University of Michigan, Ann Arbor, MI 48109. PG 12. PR No Charge. JE 022, 323, 313. KW Tax Policy. International Portfolio Diversification. Domestic Securities. AB It has been widely observed that investors' financial portfolios seem to be overly concentrated in domestic securities, despite the beneficial reduction in risks that are possible from international portfolio diversification. See for example, Feldstein and Hartman (1979), Obstfeld (1985), and Summers (1985). Indeed, government tax policy in most countries seems to actively discourage international diversification.

PD August 1987. TI Three Papers on Revealed Preference. AA University of Michigan. SR University of Michigan Center for Research on Economic and Social Theory Working Paper: 87-28; Department of Economics, University of Michigan, Ann Arbor, MI 48109. PG 5. PR No Charge. JE 022. KW Subset Of Goods. Portfolio Choice. Risk Aversion. Nonparametric. Optimizing Behavior. AB 1. Suppose that you observe n choices of k goods and prices when the consumer is actually choosing from a set of k + 1 goods. Then revealed preference theory puts essentially no restrictions on the behavior of the data. This is true even if you also observe the quantity demanded of good k + 1, or its price. The proofs of these statements are not difficult. 2. This paper derives necessary and sufficient conditions for Arrow-Debreu choices of contingent consumption to be compatible with the maximization of a state independent expected utility
function that exhibits increasing or decreasing absolute risk aversion, or increasing or decreasing relative risk aversion. The conditions can be used to bound different measures of risk aversion based on a single observation of Arrow-Debreu portfolio choice. Revealed preference analysis provides a definitive method to test for optimizing behavior. However, it has been criticized because it fails to allow for approximate satisfaction of optimizing behavior. In this note, I describe some possible solutions to this problem.

I examine a simple model of rent seeking behavior in order to determine the correct way to measure welfare loss due to rent seeking. I conduct this analysis using a general equilibrium version of the standard partial equilibrium consumers' surplus cost-benefit setup. I conclude that the ordinary tools of cost-benefit analysis, such as consumers' and producers' surplus are up to the task of measuring the deadweight loss due to rent seeking, as long as they are applied in the proper general equilibrium context.

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of a Process of Allocating Private Rights to the Use of Public Property. AU Guler, Kemal; Plott, Charles R.; Vuong, Quang H.

Wadhwani, Sushil B.

Wadsworth, Jonathan
TI Unemployment and the Inter-Regional Mobility of Labour. AU Pissarides, Christopher A.; Wadsworth, Jonathan.

Wagner, Helmut

AB There is a common understanding in economics today that there are only transitory effects of monetary policy on employment. Here I develop the theoretical rationale for the possibility of an economy's getting stuck in long-run involuntary unemployment as a consequence of a purely monetary disinflation policy. Involuntary unemployment persists despite flexible wages and prices and despite rational behavior of economic subjects. The underlying mechanism consists first of a governmental insurance policy against re-igniting inflation expectations and second of an information dilemma, or prisoner's dilemma, in which the entrepreneurs are caught. A falling interest rate—caused by an ending of the disinflation policy—is, per se, not a sufficient incentive to expand production for an individual entrepreneur. There is no functional element such as "the economy" reacting in a homogeneous way. It is rational for the single entrepreneur to wait for the others to invest first. In this case, only demand policy can get the economy out of unemployment.

Walsh, Carl E.

AB This paper attempts to assess empirically the impact on output and inflation of monetary policy in the U.S. during the period of M1 targeting from 1976 to 1984. The impact of policy shocks on output and inflation, and the impact of aggregate demand, aggregate supply and money demand shocks on M1 and the Fed's target path, are examined through the use of impulse response functions. These response functions are based on an orthogonalisation of VAR residuals derived from an estimated structural model. The VAR specification reflects the finding that M1 and the Fed's target for M1 are cointegrated. The evidence suggests that money supply shocks and shocks to M1 target have accounted for little of the observed volatility of output or inflation. However, the induced policy response to aggregate demand and supply shocks has contributed to subsequent inflation.

Warshawsky, Mark J.

AB Any analysis of the financial health of pension plans and of appropriate regulatory responses depends critically on accurate information about the nature and amount of plan liabilities. This study briefly reviews the regulatory, institutional, and economic factors relevant to pension plan obligations. It surveys the literature on the appropriate conceptual framework for measuring pension obligations and summarizes financial accounting standards for calculating and reporting the liability of a pension plan. The study describes, on reported and adjusted bases, the recent funded status (measured by the ratios of assets to liabilities) of a large sample of private pension plans. And it explains how minimum and maximum funding standards are calculated under rules set forth by the Employee Retirement Income Security Act (ERISA), how these standards influence funded ratios, and how some recent proposals could change funding standards.

Webb, Katherine W.
PD June 1986. TI Spinoffs: Applying Historical Examples to the Present. AA The Rand Corporation. SR Rand Paper: P-7322; The Rand Corporation, 1700 Main Street, PO Box 2138, Santa Monica, CA 90406-2138. PG 54. PR No Charge. JE 621, 114. KW SDL Research and Development.

AB To begin to understand how to assess the spinoff potential of the Strategic Defense Initiative, this paper examines other research and development (R&D) programs, investigating both new products and new processes. Programs examined include Apollo and other National Aeronautics and Space Administration (NASA) programs, government demonstration projects, CERN, the Manhattan Project, and military R&D. The research results indicate that (1) industries that are closely involved in both government and commercial efforts seem more likely to transfer scientific research; (2) NASA has encouraged commercial spinoffs, but other benefits include management techniques and quality control procedures; (3) an important spinoff is the training of scientists and engineers; and (4) demonstration projects may lead to spinoffs even if the primary system is not adopted.

Weber, Guglielmo
TI Intertemporal Substitution, Risk Aversion and the

Weber, Shlomo
TI Price Discrimination and Product Line Rivalry. AU Ginsburgh, Victor; MacLeod, Bentley; Weber, Shlomo.

TI Price Discrimination and Product Line Rivalry. AU Ginsburgh, Victor; MacLeod, Bentley; Weber, Shlomo.

Weil, David
TI The Worldwide Change in the Behavior of Interest Rates and Prices in 1914. AU Barsky, Robert; Mankiw, Shlomo.

AU Ginsburgh, Victor; MacLeod, Bentley; Weber, Shlomo.

TI Price Discrimination and Product Line Rivalry. AU Ginsburgh, Victor; MacLeod, Bentley; Weber, Shlomo.

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AU Ginsburgh, Victor; MacLeod, Bentley; Weber, Shlomo.

TI Price Discrimination and Product Line Rivalry. AU Ginsburgh, Victor; MacLeod, Bentley; Weber, Shlomo.
explain two puzzling facts: (1) the variability of manufacturing data suggests that order backlogs may help Inventories.

low, built up when demand is high.

production appears to be greater than that of demand, and

TI Stock Market Volatility. AU Davis, Carolyn D.;
White, Alice P.

TI Endogenous Price Fluctuations on Incomplete Markets. AA Department of Economics, University of Western Ontario and University of Bonn. SR University of Western Ontario Department of Economics Research Report: Number 76706; Department of Economics, Social Sciences Center, University of Western Ontario, London, Ontario, CANADA N6A 5C2. PG 30. PR $5.00 Canada; $7.00 Elsewhere. JE 131, 021.


AB Excessive price variability on asset markets is usually explained by exogenous factors such as expected changes in the relevant environment. In contrast to this, the model underlying this paper allows for endogenously generated price fluctuations. The basic idea is that the information gathering process itself may give rise to price fluctuations. An appropriate equilibrium concept is introduced and conditions for the existence of such equilibrium are discussed.


AB A discrete, dynamic general equilibrium model of asset pricing is constructed in which equilibrium prices are influenced by exogenously given stochastic information signals, and by the endogenously generated price function prevailing in the respective preceding period. This structural assumption and its consequences for the informational efficiency of the markets are discussed extensively. The implications for explaining price volatility are also explored. In addition to that, the model allows the investigation of a novel issue: learning from price fluctuations. It is shown that sophisticated agents can obtain additional information from stable cycles of equilibrium price functions. The resulting change in the equilibrium structure might induce a rational expectations equilibrium, as illustrated by means of an example.

TI Ex Post Versus Ex Ante Optimal Policies for Risky Activities. AU Bovdy, Robin W.; Wildasin, David E.


TI Existence of General Equilibrium in a Competitive Economy with Endogenous Credit Rationing. AU Kamiya, Kazuya; Wildasin, David.

TI The War of Attrition in Continuous Time With Complete Information. AU Hendricks, Ken; Weiss, Andrew; Wilson, Charles.


TI Decentralised Trading, Strategic Behavior and the Walrasian Outcome. AU Rubinsteir, Ariel; Wolinsky, Asher.

TI The External Debt Situation in Indonesia: Performance and Prospects. AA University of California at Davis. SR University of California at Davis Research Program in Applied Macro and Macro Policy: 48; Department of Economics, University of California at Davis, Davis, CA 95616. PG 32. PR No Charge. JE 121, 431, 441, 023. KW Debt Crisis. Indonesia. Exchange Rate. Political Economy.

AB In interviews with bankers, government economists and academic observers, most of them attributed the absence of an Indonesian debt crisis during 1982-84 to the fact that a significant portion of external public debt, an average of 37 percent, was long-term concessionary loans from foreign governments and international agencies. Our analysis challenges this conventional explanation. We show that if Indonesia (1) had paid the same effective interest rate as Mexico, (2) had the same maturity structure as Mexican debt, and (3) had the same export-GNP ratio as Mexico, then its average 1980-82 total debt service-export ratio would have been 84.4 per cent instead of the actual 30.1 per cent. We have therefore concluded that the major cause for the favorable 1982-84 outcome is competent management of the exchange rate. In the last section, we recommend an aggressive exchange rate policy and two sets of supplementary measures to reduce the probability of a debt crisis in the medium run.

TI The Core of a Market with a Continuum of Players and Finite Coalitions: From Finite to Continuum Economies. AU Kaneko, Mamoru; Wooders, Myrna Holtz.

(Economics Series) Technical Report: TR503; Institute for
Mathematical Studies in the Social Sciences, Encina Hall,
Fourth Floor, Stanford University, Stanford, CA 94305.
PG 57. PR $4.00. JE 026, 021. KW NTU Value.
Core. Non-transferable Utility.
AB We show that the well-known value convergence
theorems for exchange economies have analogs in a
framework which is sufficiently broad to encompass diverse
economic situations. The framework we use is that of
NTU games (i.e., cooperative games without
sidepayments). Our central result is that, for a large
game, all NTU values satisfying a mild symmetry
condition are in an approximate core. We also obtain an
ordinal version of this result.

Yamada, Tadashi
PD November 1987. TI Nutrition and Infant Health
in Japan. AU Yamada, Tadashi; Yamada, Tetsuji;
Chaloupka, Frank. AA Chaloupka and Yamada,
Yamada, Tetsuji: Rutgers University. SR National
National Bureau of Economic Research, 1050
Massachusetts Avenue, Cambridge, MA 02138.
AB The model presented in this paper emphasizes the
importance of the mother's nutritional intake as a
determinant of infant health. Using cross-sectional market
averages for 1980 and 1981 in Japan, we find that the
nutrient intake of the mother during pregnancy is a
potential determinant of neonatal and infant mortality in
Japan, with increased consumption of calcium and iron
leading to improved birth outcomes. Using the results
obtained from the estimation of neonatal and infant
mortality production functions, we note that increases in
the prices of food items, in particular milk and meat,
would lead to increases in neonatal and infant mortality
rates. We discover that the availability of abortion in
Japan, unlike in the United States, is positively related to
mortality rates, although never significantly. Finally, we
see that cigarette smoking, alcohol consumption, and poor
environmental quality all have strongly adverse effects on
newborn survival outcomes in Japan.

TI Social Security and Earlier Retirement in Japan:
Cross-Sectional Evidence. AU Yamada, Tetsuji;
Yamada, Tadashi.

Yamada, Tetsuji
TI Nutrition and Infant Health in Japan.
AU Yamada, Tadashi; Yamada, Tetsuji; Chaloupka,
Frank.
PD November 1987. TI Social Security and Earlier
Retirement in Japan: Cross-Sectional Evidence.
AU Yamada, Tetsuji; Yamada, Tadashi; AA Yamada,
Tetsuji: Rutgers University. Yamada, Tadashi: National
Bureau of Economic Research. SR National Bureau of
Bureau of Economic Research, 1050 Massachusetts
Avenue, Cambridge, MA 02138. PR $2.00. JE 915, 918, 821,
AB The estimated elasticity of the probability of
retirement with respect to social security retirement
benefits declines as individuals age. The negative impact
of social security retirement benefits on full-time workers is
much greater than the impact on part-time workers for all
age groups. Earnings test in Japan is, therefore, more
effective on full-time workers than part-time workers
among the elderly. Social security retirement benefits also
provide the elderly with an incentive to prolong their
unemployment status. The marginal effect of the market
unemployment rate on full-time work is significantly larger
than that on part-time work and both effects are negative.
The elasticity of retirement with respect to the market
unemployment rate for those in their 60's is two to three
times larger than those aged 70 and over. Retirement of
those in their 60's is quite responsive to changes in labor
market condition.

Yancey, Thomas
TI Power and Pre-Test Risk Comparisons for
Conventional and Joint One Sided Tests. AU Judge,
George; Bohrer, Robert; Yancey, Thomas.

Young, Robert A.
PD July 1987. TI Canada - United States Free Trade:
Economic Realities and Political Choices.
AA Department of Political Science, University of
Western Ontario, SR University of Western Ontario
Centre for the Analysis of National Economic Policy
Working Paper: 87-03; Department of Economics, Social
Sciences Center, University of Western Ontario, London,
Ontario, CANADA N6A 5C2. PG 46. PR No Charge.
JE 421, 422, 423, 122. KW Politics. Trade Policy.
Protectionism. Bilateral Agreement. Canada. United
States.
AB Political choice is worth emphasizing now for three
reasons, which also constitute the central themes of this
paper. Advocates of all sorts of initiatives resort to the
banal argument that their favoured option is inevitable or
unavoidable; hence, the first part of the discussion shows
that a Canada-United States free-trade agreement is not in
this strict sense necessary. Second, the Canadian debate
threatens to become terribly bitter. The degree of division
will depend on the scope of the agreement, so Part III of
this paper analyses the forces which will determine the
choice between a limited, incremental deal and one which
is comprehensive and daring and which takes continental
economic integration to new levels. Finally, if some
bilateral agreement is likely to emerge, a precise
touchstone for assessing it is essential. In my view, this
touchstone should derive from the goal of maximizing the
range for political choice, while securing the economic base
without which sovereignty is meaningless. Assessing a deal
means asking whether its terms will neutralize the policy
instruments necessary for development over the next
several decades. Within the constraints of an agreement,
in short, can Canadians secure their culture, operate
desirable social programs, and implement essential
industrial policies? This question is approached in Part IV
through an analysis of Rick Harris's work for the
Macdonald Commission, and this leads at last to
predictions about the outcome of the issue.

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Zame, William R.
TI The Regularity of Business Cycles. AU Wooders, Myrna; Zame, William R.

Zarnowitz, Victor
AB Do business cycles have predictable periodicities or are they random walks without past regularities or predictive value? Arguments in support of either position are found in the literature, with no apparent convergence to an agreement. This paper first examines the implications of the NBER chronologies and other findings for the question of the regularity of business cycles. It discusses hypotheses and presents evidence concerning the incidence and coexistence of cycles with different periods. An extension of the analysis covers growth cycles in the United States and other major countries. The paper then considers different models — linear, nonlinear, endogenous, and exogenous — for what they have to say about the problem. The regularity of investment cycles and the possible asymmetries in cyclical behavior receive particular attention, and some related data and tests are provided. Our results suggest that business cycles defy simple characterizations: they show a strong tendency to recur and at times even near periodicity, along with great diversity and evolution of phase durations. The age of a phase is not of much help in predicting the date of its end; the regularities are mainly in the dynamics of the developing business conditions.

Zeckhauser, Richard
TI The Dilemma of Government Responsiveness. AU Rodrik, Dani; Zeckhauser, Richard.

Zeldes, Stephen P.
TI Production, Sales, and the Change in Inventories: An Identity that Doesn't Add Up. AU Miron, Jeffrey A.; Zeldes, Stephen P.
TI Seasonality, Cost Shocks, and the Production Smoothing Model of Inventories. AU Miron, Jeffrey A.; Zeldes, Stephen P.
TI Seasonality, Cost Shocks, and the Production Smoothing Model of Inventories. AU Miron, Jeffrey A.; Zeldes, Stephen P.

Zilberman, David
TI Computer Use in Agriculture: Evidence from Tulare County, California. AU Putler, Daniel S.; Zilberman, David.

Zilcha, I.
AB This is an extension of Diamond's (1965) model which includes stochastic production. We obtain a complete characterization of inefficient feasible production consumption allocations. Existence of competitive equilibrium is proved and it is shown that it is short-run efficient. Also any efficient allocations (of type II) can be obtained as a competitive equilibrium for some concave utility functions for all generations.
TI Efficient Sets With and Without the Expected Utility Hypothesis. AU Safr, Zvi; Zilcha, Itzhak.

Zin, Stanley E.
AB The empirical rejections of life cycle models of aggregate consumption are reviewed and an alternative specification is proposed. In a representative agent, rational expectations equilibrium framework, the maximization of a non-additive recursive utility index yields restrictions on the time series behaviour of aggregate per capita consumption. It is shown that empirical rejections of the conventional additive utility model are not necessarily rejections of these restrictions. Non-additive recursive utility has found frequent use in dynamic economic models because of the non-constancy of time-preference that it embodies and the more general long run behaviour that it can generate. This model, therefore, provides a framework for testing hypotheses about both life cycle consumption behaviour and the nature of time-
preference. Observable implications of Euler equations are used to estimate the parameters of the utility function using Generalized Method of Moments and the asymptotic properties of this estimator are analyzed when the consumption process is nonstationary. The model is estimated and tested using monthly United States post-war data and the time-additivity restriction is rejected. When consumption is measured by aggregate per capita expenditures on nondurable goods, the overidentifying restrictions of the model cannot be rejected at conventional significance levels. However, this is not the case for a consumption measure that includes expenditures on services. The empirical results generally provide support for the "increasing marginal impatience" hypothesis that posits an increasing relationship between the rate of time preference and steady-state consumption (or wealth).

PD July 1987. TI Intertemporal Substitution, Risk and the Time Series Behaviour of Consumption and Asset Returns. AA Queen's University. SR Queen's Institute for Economic Research Discussion Paper: 694; Department of Economics, Queen's University, Kingston, Ontario, CANADA K7L 3N6. PG 36. PR $3.00 Canada and United States; $3.50 Foreign. JE 023, 212, 313. KW Consumption. Asset Returns. Risk Aversion. Non-Expected Utility. Ordinal Certainty Equivalent. AB This paper studies the time series behaviour of aggregate consumption and asset returns when the representative agent does not (necessarily) maximize the expected value of a von Neumann-Morgenstern utility index. By assuming that agents' intertemporal preferences over stochastic consumption sequences have the multiperiod analogue of the Ordinal Certainty Equivalent representation of Selden (1978, 1979), testable implications for the joint behaviour of consumption and asset returns are derived. These preferences contain the conventional von Neumann-Morgenstern representation as a special case and have the attractive property of allowing for "risk preference" and "time preference" to be modelled independently. It is shown that, for this model, the result in Hansen and Singleton (1983) that the serial correlation properties of asset returns are related to the stochastic properties of consumption by the degree of risk aversion, no longer holds. The result in Hall (1981, 1985) linking this relationship to the intertemporal elasticity of substitution (which is allowed to be independent of the degree of risk aversion) is, however, confirmed. Issues involving the intertemporal consistency of optimal plans are briefly discussed. The model is estimated and tested using monthly United States data on non-durable consumption, treasury bill returns, and corporate bond returns.

TI Substitution, Risk Aversion and the Temporal Behavior of Consumption and Asset Returns I: A Theoretical Framework. AU Epstein, Larry G.; Zin, Stanley E.

TI Substitution, Risk Aversion and the Temporal Behaviour of Consumption and Asset Returns II: An Empirical Analysis. AU Epstein, Larry G.; Zin, Stanley E.

TI Testing a Government's Present-Value Borrowing Constraint. AU Smith, Gregor W.; Zin, Stanley E.

Zinde, Walsh Victoria

TI Inflation and the Timing of Price Changes. AU McMillan, John; Zin, Walsh Victoria.