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Abstracts

Is Growth Exogenous? Taking Mankiw, Romer, and Weil Seriously

BEN S. BERNANKE AND REFET S. GÜRKAYNAK

Is long-run economic growth exogenous? To address this question, we show that the empirical framework of Mankiw, Romer, and Weil (1992) can be extended to test any growth model that admits a balanced growth path, and we use that framework both to revisit variants of the Solow growth model and to evaluate simple alternative models of endogenous growth. To allow for the possibility that economies in our sample are not on their balanced growth paths, we also study the cross-sectional behavior of total-factor-productivity growth, which we estimate using alternative measures of labor's share. Our broad conclusion, based on both model estimation and growth accounting, is that long-run growth is significantly correlated with behavioral variables such as the savings rate, and that this correlation is not easily explained by models in which growth is treated as the exogenous variable. Hence, future empirical studies should focus on models that exhibit endogenous growth.

Long-Term Capital Movements

PHILIP R. LANE AND GIAN MARIA MILESI-FERRETTI

International financial integration allows countries to become net creditors or net debtors with respect to the rest of the world. In this paper, we show that a small set of fundamentals—shifts in relative output levels, the stock of public debt, and demographic factors—can do much to explain the evolution of net foreign-asset positions. In addition, we highlight that "external wealth" plays a critical role in determining the behavior of the trade balance, both through shifts in the desired net foreign-asset position and through the investment returns generated on the outstanding stock of net foreign assets. Finally, we provide some evidence that a portfolio balance effect exists: real interest-rate differentials are inversely related to net foreign-asset positions.

Do We Really Know that Oil Caused the Great Stagflation? A Monetary Alternative

ROBERT B. BARSKY AND LUTZ KILIAN

This paper argues that major oil price increases were not nearly as essential a part of the causal mechanism that generated the stagflation of the 1970s as is often thought. There is neither a theoretical presumption that oil supply shocks are stagflationary nor robust empirical evidence for this view. In contrast, we show that monetary expansions and contractions can generate stagflation of realistic magnitude even in the absence of supply shocks. Furthermore, monetary fluctuations help to explain the historical movements of the prices of oil and other commodities, including the surge in the prices of industrial commodities that preceded the 1973–1974 oil price increase. Thus, they can account for the striking coincidence of major oil price increases and worsening stagflation.

The Cost Channel of Monetary Transmission

MARVIN J. BARTH III AND VALERIE A. RAMEY

This paper presents evidence that the *cost channel* may be an important part of the monetary transmission mechanism. We first highlight three puzzles that might be explained by a cost channel of monetary transmission. We then provide evidence on the importance of working capital and argue why monetary contractions can affect output through a supply channel as well as the traditional demand-type channels. Using a vector autoregression analysis, we investigate the effects across industries. Following a monetary contraction, many industries exhibit periods of falling output and *rising* price–wage ratios, consistent with a supply shock. The effects are noticeably more pronounced during the period before 1979.

The 6D Bias and the Equity-Premium Puzzle

XAVIER GABAIX AND DAVID LAIBSON

If decision costs lead agents to update consumption every D periods, then econometricians will find an anomalously low correlation between equity returns and consumption growth (Lynch, 1996). We analytically characterize the dynamic properties of an economy composed of consumers who have such delayed updating. In our setting, an econometrician using an Euler equation procedure would infer a coefficient of relative risk aversion biased up by a factor of $6D$. Hence with quarterly data, if agents adjust their consumption every $D=4$ quarters, the imputed coefficient of relative risk aversion will be *24 times greater* than the true value. High levels of risk aversion implied by the equity premium and violations of the Hansen–Jagannathan bounds cease to be puzzles. The neoclassical model with delayed adjustment explains the consumption behavior of shareholders. Once limited participation is taken into account, the model

matches most properties of aggregate consumption and equity returns, including new evidence that the covariance between $\ln(C_{t+h}/C_t)$ and R_{t+1} slowly rises with h.

Evolving Post–World War II U.S. Inflation Dynamics

TIMOTHY COGLEY AND THOMAS J. SARGENT

For postwar U.S. data, this paper uses Bayesian methods to account for the four sources of uncertainty in a random coefficients vector autoregression for inflation, unemployment, and an interest rate. We use the model to assemble evidence about the evolution of measures of the persistence of inflation, prospective long-horizon forecasts (means) of inflation and unemployment, statistics for testing an approximation to the natural-unemployment-rate hypothesis, and a version of the Taylor rule. We relate these measures to stories that interpret the conquest of U.S. inflation under Volcker and Greenspan as reflecting how the monetary policy authority came to learn an approximate version of the natural-unemployment-rate hypothesis. We study Taylor's warning that defects in that approximation may cause the monetary authority to forget the natural-rate hypothesis as the persistence of inflation attenuates.