

Savings and the Financial Underpinnings of Macro Models



Workshop Vision Statement

The Savings and Financial Underpinnings of Macro Models Workshop, which is supported by CFSP, is interested in the role that savings and financial institutions play in enhancing the welfare and well-being of households. Thus we look at the impact of financial services not only directly on households themselves, but also indirectly, through growth, employment, price movements and other economy-wide changes. We bring together development economists and researchers, who are working on quantitative micro-founded macroeconomic models and who have relevant technical expertise in a variety of sub-fields, in order to build better, more relevant models that have realistic financial underpinnings. Our goal is to better understand the impact of savings and related financial innovations through these models. This includes examining more comprehensive feedback effects across markets, their impact through economic development, and shifts in distribution of income.

Models allow us to answer specific counterfactual questions. For example, we can examine the impact of electronic payments when lowering the costs of spatial separation and enhancing economic integration of poor people into the financial system. In this sense, models are complementary with experiments such as those conducted in randomized control trials (RCT), but models have at least two significant advantages.

First, with realistic parameters, estimated or calibrated, researchers can analyze the impact of a policy change that includes general equilibrium effects. That is, they allow researchers to understand the economy-wide consequences of scaling up particular development policies at low cost, avoiding unintended social consequences. Second, models allow researchers to assess the impact of counterfactuals; that is, they can examine policies that have never been implemented but may be under consideration. Models allow more flexibility at the time of designing and exploring policy alternatives, avoiding the onerous cost associated with the evaluation of a myriad of individual interventions after the fact.

We expect that The Savings and Financial Underpinnings of Macro Models Workshop will integrate and challenge various, usually disconnected, areas in economic development and the macroeconomics of financial intermediation.

Traditionally, development economics has focused on the partial equilibrium phenomenon. For example, researchers study how policy treatments such as subsidies to financial institutions to cover costs or enhanced interest rates to potential savers can increase financial access compared to those who were untreated. However, when savings is mobilized from a low wealth population, at a large scale as is hoped for, the amounts, in aggregate, can cause an additional impact on the

local, regional, or even national economies, depending on the application. Specifically, intermediation of increased savings (through on-lending) can impact interest rates, factor prices, occupational choices and sectoral development. These kinds of general equilibrium effects can contribute substantially to the distribution of gains from a policy innovation, and for that matter, to the distribution of losses for some, as well. Therefore, evaluation of large-scale phenomena requires general equilibrium models with realistic financial sectors.

Macroeconomic growth models using the representative agent framework, which have been used to study economy-wide movements of aggregate variables, are not entirely suitable, either. In particular, such models are silent about poverty and distributional considerations. More broadly, they miss the integration of imperfect, but potentially changed, financial systems with the macro-economy. Imperfect financial integration among people is known to be a key force underneath poverty dynamics and inequality movement, so changed financial systems can impact all these variables as well as economy wide growth.

There is, however, a more relevant macro literature featuring models of heterogeneous agents and explicit financial sectors. Mostly these models are used to study questions in advanced economies, especially the U.S. economy, e.g., causes and consequences of financial crises. Lately there is also work on the industrial organization of banks not only over business cycle frequencies in the U.S., but also tracking the longer term, secular impact in OECD countries of the expansion of the financial sectors. We plan to mobilize this modeling expertise and leverage it to applications in emerging market economies and also to those more stagnant, poor economies that are not growing.

We are already making progress. These new models can be used to study the impact of financial liberalization on growth and on the distribution of income. Similarly, the models can incorporate the informal sector and a less-than-adequate formal sector, in order to then assess the impact of lowering the costs of access and improving formal sector products. Other potential research examples include: to what extent do shocks to financial intermediation in developing countries drive fluctuations, and can that instability be remedied? To what extent does the expansion of financial service providers drive growth and how can the welfare impact of that growth be enhanced?

The Savings and Financial Underpinnings of Macro Models Workshop recognizes the need to bridge partial equilibrium, macroeconomic growth, and rich heterogeneous agent models by constructing general equilibrium models that allow both the observed heterogeneity in people and actual, measured financial frictions. Indeed, theories need to be checked against the data for plausibility, and ideally estimation, both at the macro and micro levels. The aims of this workshop are to foster interest in research in the financial systems of developing countries and, above all, to assist in the development of theories and empirical strategies that can be used to evaluate the impact of financial sector change.

Participants

Juan Pablo Xandri Antuna
PhD student
Massachusetts Institute of Technology

Juliano Assunção
Assistant Professor of Economics
Pontifícia Universidade Católica do Rio de Janeiro

Joaquin Blaum
PhD student
Massachusetts Institute of Technology

Francisco Buera
Assistant Professor of Economics
University of California Los Angeles

Stijn Claessens
Assistant Director
Research Department, IMF

P. Dean Corbae
Rex A. and Dorothy B. Sebastian Centennial
Professor in Business Administration
University of Texas, Austin

Pablo D'Erasmus
Assistant Professor of Economics
University of Maryland, College Park

Jeremy Greenwood
Professor of Economics
University of Pennsylvania

Fatih Guvenen
Assistant Professor of Economics
University of Minnesota

Chang Tai Hsieh
Professor of Economics
University of Chicago Booth School of Business

Felipe Iachan
PhD student
Massachusetts Institute of Technology

Roberto Fattal Jaef
PhD student
University of California Los Angeles

Anil K. Jain
PhD student
Massachusetts Institute of Technology

Joseph Kaboski
Associate Professor of Economics
Notre Dame University

Greg Kaplan
Assistant Professor of Economics
University of Pennsylvania

Amir Kermani
PhD student
Massachusetts Institute of Technology

Kyungmin Kim
PhD student
Massachusetts Institute of Technology

Nobuhiro Kiyotaki
Professor of Economics
Princeton University

Guido Lorenzoni
Pentti Kouri Associate Professor of Economics
Massachusetts Institute of Technology

Alisdair McKay
Assistant Professor of Economics
Boston University

Michael Peters
PhD student
Massachusetts Institute of Technology

Roberto Rigobon
Professor of Economics
Sloan School of Management
Massachusetts Institute of Technology

Juan Sanchez
Economist
Federal Reserve Bank of Richmond, Virginia

Yongs Shin
Assistant Professor of Economics
Washington University in St. Louis

Ken Singleton
Adams Distinguished Professor of Management
Stanford Graduate School of Business

Narapong "White" Srivisal
PhD student
University of Chicago

Tavneet Suri
Mitsubishi Career Development Assistant Professor
of International Management
Sloan School of Management
Massachusetts Institute of Technology

Robert M. Townsend
Elizabeth and James Killian Professor of Economics
Massachusetts Institute of Technology

Christopher Udry
Henry J. Heinz II Professor of Economics
Yale University

Kenichi Ueda
Senior Economist
Research Department, IMF

Christopher Woodruff
Associate Professor of Economics
University of California San Diego