Research Themes in Behavioral Macroeconomics

Language: English

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Course Information

Course Prerequisites:
Good knowledge and Microeconomics and Macroeconomics. A basic knowledge of a numerical programming language (such as Matlab or R) is desirable.

Course Content:

Macroeconomic outcomes depend on how expectations are formed by individuals in the economy. Behavioral macroeconomics seeks to model expectations following realistic aspects of human behaviour aiming to be more realistic than the theoretically sophisticated rational expectations macroeconomics, which assumes intertemporal optimization by hyper-rational individuals. It is well known that human behaviour gets shaped by psychological factors such as cognitive biases, time-inconsistency, and social status. All this casts doubt on the rational expectations paradigm, which was subject to a great criticism after the eruption of the financial crisis in 2007.

To avoid the risk of models in which anything is possible and all can be fit and nothing predicted, it is necessary to replace the assumption of rational expectations only with alternative assumptions which are based on empirical psychological research. This means that behavioral models must be simple and stylized and can't consider all forms of irrationality which we know (from introspection and experience) afflict us.

In particular, this course will consider the macroeconomic implications of the well documented fact that when faced with a random walk, people make forecasts which would be appropriate if they faced a stationary process around a broken trend. This means they alternate between assuming that unusual observations are followed by reversion to the old trend and extrapolating recent changes.

Course Structure:

The course will consist of 6 lectures, for a total of 12 hours.

Course Literature:
The textbook is


In the course will also use research articles and working papers

Andreasson and Krause (1990) "Judgmental Extrapolation and the Salience of Change"


Barberis, Shleifer, and Vishny (1998) "A model of investor sentiment"


*Additional Information:*

The Course Content will cover:

1. Introduction & some useful tools
2. Expectations with under-reaction and over-reaction
3. Modelling economic choices with limited understanding of subjective expectations
4. A behavioral macroeconomic model vs a standard new keynesian macroeconomic model.
5. A behavioral macroeconomic model with a representative agent vs a model with a diversity of opinions (this can make little difference)
6. A behavioral macroeconomic model with a diversity of opinions and liquidity constraints (this can make a huge difference).

The course will be graded based on a research paper of not more than 10 pages.

This outline is based on that of an earlier course taught by Guido Cozzi.