

Index

- Abadir, K. M. 140 n.
accelerator mechanisms 21
accounting identities 23, 74–5
ADF (Augmented Dickey-Fuller) test 200–1,
 203
adjustment costs 5, 22, 42
 dynamics of models 46–8
 LQ optimisation models involving 38, 89
adjustment mechanisms 21
Adolfson, M. 29 n.
aggregation 22, 42
AIC (Akaike Information Criterion) 85, 108,
 163, 198, 204, 218, 219, 221, 268, 269,
 270, 271, 272, 273
Akerlof, G. 100
Akusawan, M. 291
alternative modelling approaches 4–6,
 24–31, 98–103, 221–3
Anderson, D. R. 163
Anderson, R. G. 290
Ando, A. 13
anti-inflationary policy 192
appreciation 75, 235, 247–8
 large initial 245
 persistent 245
 sterling 188–9
approximations 17, 131, 161
 log-linear 45, 81
arbitrage conditions 6, 23, 28, 67, 71–4, 97,
 233
ARMA (autoregressive moving average) 48,
 204 n., 218
 benchmark 219, 221
 univariate 219
 unrestricted 219
 see also VARMA
Asian crisis (1997) 291, 296
asset-income ratios 23, 28
asset markets 233
asset revaluation term 75 n.
assets:
 financial 74, 76, 77, 80
return on 72, 78
see also foreign assets
Astley, M. 18, 54
asymptotic distributions 123, 138 n., 209
Australia 13, 290
autoregressive models 83
see also ARMA; BVAR; GVAR; VAR;
 VARMA; VARX
Bakhshi, H. 100 n.
Banerjee, A. 105 n.
Bank of Canada 29 n., 291
Bank of England 14, 15 n., 89 n., 274
 ‘Competition and Credit Control’
 publication 192
inflation and output growth forecasts
 263 n.
Inflation Report 274–5
inflation targets 8, 10, 98
operational independence 181 n.
remit of 100 n.
bankruptcies 303, 304
Barassi, M. R. 266
Barrell, R. 15 n.
Barro, R. J. 69, 93 n., 233
base rate 89, 102, 227
 changing 95, 96, 99
 derivation of 92–4
 reaction function 94–7
baskets of goods/commodities 71, 72
Bayesian techniques/method 23, 29, 30,
 109, 155, 156, 292
DSGE models 18
predictive density 157
see also BMA; BVAR; SBC
behavioural relationships 4, 5, 15
 identification of 3
 underlying 53
benchmark models 218–21, 266, 268, 270,
 271, 272, 285, 286
 over-identified 273
Berkowitz, J. 272 n.

Bernanke, B. S. 18, 52, 53, 91 n., 92 n., 233 n., 261
 Bernard, A.B. 211
 Binder, M. 20 n., 42, 45, 47, 69
 Bjørnstad, J. F. 156 n., 162
 Blake, A. P. 263 n.
 Blanchard, O. J. 4, 18, 19, 50–1, 54, 55
 Blinder, A. S. 52, 53, 92 n.
 Blundell, R. 46
 BMA (Bayesian Model Averaging) 158–9, 160, 161, 162, 266, 268
 BN (Beveridge-Nelson) decomposition 248, 249, 257–8
 relationship of GRW and 250–2
 Bodkin, R. G. 14 n.,
 bonds 74, 290
 foreign 76, 77
 bootstrapping exercises/procedure 140, 141, 166, 167, 208, 302
 non-parametric technique 269
 predictive density 156
 Box-Jenkins methodology 218
 Brand, C. 290
 Branson, W. H. 76
 Brayton, F. 13, 14 n., 16
 Breeden, F. J. 211
 Breson, G. 46
 Britton, E. 263 n.
 Brunner, A. D. 52
 Bruno, M. 72 n.
 bubble effects 20
 budget constraints 14
 Buiter, W. 78 n.
 Bullard, J. 54
 Burnham, K. P. 163
 Busetti, F. 177 n.
 business cycles
 effect of shocks to financial markets on 62
 highly synchronised 259
 monetary factors influencing 22
 see also RBC
 BVAR (Bayesian autoregressive) models 4, 18

 calibration exercises 22
 Callaghan government (UK) 181, 193
 Calvo, G. 23
 Campbell, J. Y. 211
 Canada 290, 297
 Canova, F. 249 n.
 capital:
 assumed to depreciate 42
 marginal product of 70
 real rate of return on 73

capital markets:
 less well-developed 294 n.
 regions without 296
 capital stock 68, 69, 100
 foreign 70
 cash portfolios 193
 Cayen, J.-P. 29 n.
 central banks 25, 29 n.
 independent 100, 181
 information available to 94
 Champnorne, D. G. 3, 105 n.
 Chatfield, C. 153 n.
 Chauduri, K. 72 n.
 Cheung, Y. W. 205
 China 15, 293, 294 n., 296
 chi-squared statistics 232
 Choleski decomposition 17, 49, 110, 114, 115, 134, 142, 167, 231
 Christiano, L. J. 5 n., 20 n., 22, 23, 29, 30 n., 42, 51, 52, 53, 54
 circulation of money 207
 Clarida, R. 18, 22, 23, 54
 Clarke, P. 249 n.
 Clemen, R. T. 159, 160
 Clements, M. P. 160 n., 266
 closed economy 42, 64, 293
 Cobb-Douglas production function 20, 43
 aggregate constant returns to scale 42
 Cochrane, J. H. 261
 coefficient matrices 118
 contemporaneous 107
 error correction 137
 loading 84, 197
 coefficients 92, 200, 236
 adjustment 35, 55, 118
 autocorrelation 17
 cointegrating 137
 correlation 256, 258, 259
 dynamic 35
 error-correction 84, 129, 137, 197, 212
 loading 227
 long-run 85, 97, 115, 137, 266, 268
 reduced-form 88, 111, 120
 restricted 115, 118
 short-run 84, 97, 264, 266
 unit, normalising 49
 unknown 117
 zero and unity 46
 see also structural coefficients; trend
 coefficients
 Cogley, J. 211
 Cogley, T. 22, 263 n.

cointegrating VAR models 6, 24, 40, 117–35, 207, 226, 253, 266
 analysis of 10, 36, 83
 augmented 7
 estimation of 62, 208, 254
 four-variable 298
 identifying long-run relationships
 embedded within 37
 region-specific 294
 relative simplicity of 8
 six-variable 290
 trend/cycle decomposition in 248–5
 see also structural cointegrating VAR
 cointegration 3, 64, 200
 cross-country/inter-country surveys 65
 multivariate models without 252
 surveys of literature on 105 n.
 cointegration analysis 129–35, 223
 investigating PPP using 210
 cointegration tests 7, 24, 198, 198, 205, 233 n., 266
 commodity prices 51, 52, 53
 COMPACT (simultaneous equation model) 291, 292 n.
 competitive equilibrium outcome 43
 computer programs 10–11
 conceptual models 29
 conditional models 58, 59
 confidence error bands 233
 consumption 42, 75
 contemporaneous relations 48–51
 contemporaneous values 51
 Cooley, T. F. 20 n., 22, 49
 Corbett, A. 29 n.
 core models 305
 monthly version 297–303
 core variables unit 25, 60, 135
 unit root properties of 200–4
 correlation 248
 correlation matrix 124
 correlations 113
 chance, with omitted variables 109
 contemporaneous 166–7
 non-zero 134
 observed, estimated reduced form errors 141
 see also serial correlation
 cost functions 28
 co-trending 7, 24, 120, 121, 211
 counter-factuals 139, 225
 covariance matrices 48, 88, 113, 116
 asymptotic 157
 non-singular 63
 positive 137, 164, 165

covariance restrictions 19 n., 54
 exactly identifying 18
 theory-based 18
 covariances:
 contemporaneous 139
 cross-country 64
 error-correction 261 n.
 significant changes in structure 236
 stationary processes 16
 Cowles Commission 3, 4, 13, 49, 51, 110
 CPI (Consumer Price Index) 274, 290
 credit cards 77, 303, 304
 credit risk modelling 292–7
 critical values 123, 140, 141, 205, 208, 266, 273 n.
 asymptotic 138 n., 199 n.
 bootstrapped 209
 Crowder, W. J. 6, 54, 290, 298
 currency:
 foreign 71, 75, 171
 reference 293
 Cussola, N. 290

 Daniel, B. C. 72 n.
 Darby, M. R. 210, 291
 David-Fletcher-Powell algorithm 208 n.
 Davidson, J. E. H. 106
 Dawid, A. P. 146, 269
 debt burden 303
 decision-making 38, 51, 56, 145, 154
 financial 303
 fine distinctions of timing in 54
 important influence on 9
 institutional detail 87
 intertemporal nature 38
 investigator's understanding of context 49
 opportunities for modelling 61
 rigidities arising in 25
 short-run 82
 decision problems 20, 146, 147, 153
 demand for complete specification of 269 n.
 decision rules 98, 227
 optimal 20
 private agents 89
 decision-theoretic approach 269
 Dees, S. 62, 292, 293, 293–4, 299
 deflationary measures 192
 DeJong, D. 18, 28
 Del Negro, M. 23, 28

demand:
 asset 76, 77, 78, 79, 80
 excess 39
 export 81, 290
 import 81, 290
 labour 46
 news likely to impact on 56
 reserves 53
see also money demand
 density function 157, 158, 161, 162, 168
 depreciation 42, 81, 82 n., 171, 181, 187, 188–9, 247
 moderate 188
 sequence of periods of appreciation followed by 245
 deterministic trends 120, 147, 148, 151, 197
 coefficients on 138 n., 211, 250
 linear 117, 119, 121, 135
 restriction 138
 de-trending 30
 explicit multivariate approach to 256
 devaluation 187
 deflationary measures to support 192
 DGP (data generating process) 157, 159, 163
 Dickey, D. A. 106, 122, 200
 Diebold, F. X. 159, 270, 272, 303
 difference-stationarity 40, 84, 101, 147
 dimensionality 18
 discount factor 43, 47
 discount rate 98, 171
 disequilibria 39, 83, 306
 credit market 305
 economically meaningful but unobservable 40 n.
 inflation 82
 interest rates 82, 97
 response to deviations from 199
 stochastic 130
 variables not affected by 56–7
 distribution functions 150
 predictive 278
see also probability distribution function
 disturbances 23, 28, 35, 84, 197, 265
 Gaussian 122
 money market 53
 reduced-form 57, 58, 81, 82, 101, 114, 226
 structural 50, 58, 82, 226
 technological 68
see also long-run disturbances
 Doan, T. 4, 18
 Dornbusch, R. 245

Draper, D. 153 n., 158, 160, 163 n.
 Drygham, P. 37
 DSGE (Dynamic Stochastic General Equilibrium) models 5, 7 n., 19–23, 27–31, 35 n.
 Bayesian techniques in 18
 dynamics of 41–6
 fully articulated, restrictions might be motivated by 89
 recent versions 38
see also New Keynesian DSGE models
 Durlauf, S. N. 211
 dynamic adjustments 14
 dynamic multipliers 110, 111
 economic fluctuations 21–2
 Ehrmann, M. 303
 Eichenbaum, M. 22, 30 n., 42, 51, 52, 53, 54, 242, 245
 eigenvalues 124, 125, 132, 253
 trace and maximum 122–3, 138 n., 140, 198, 204–5
 EMU (Economic and Monetary Union) 291
 endogenous variables 34 n., 57, 83, 109, 111, 117, 135, 203, 219, 227, 236, 236, 246, 300
 cointegrating 107
 distinction between exogenous and 4, 49, 56, 169
 effects on 114
 estimates of impulse response functions of 231
 future values of 65, 110
 instantaneous interactions between 107
 interactions between exogenous and 139
 lagged changes in 84
 measured effect of typical shock on 115
 number and list to be included 108
 permanent/transitory decomposition of 249
see also VARX models
 Engle, R. 3, 14, 118 n.
 equal weights 268, 269, 270
 equations 218
 determinantal 46, 107
 error-correction 212, 223, 266
 estimated error correction 266
 foreign interest rate 239–41
 foreign output 236–9
 log-linear 23, 78
 non-linear 44

oil price 232, 268
 regional 64
 structural 58, 59, 97, 99, 102, 227, 229
see also Euler equations; SEMs
 equilibria 14, 20
 deviations from 35, 39–40, 118
 long-run 233
 monetary 242
 slow speed of convergence towards 233
 stock-flow 67, 80
 equilibrium relationships 76, 79
 long-run 81
 ergodicity 28, 70, 73, 76
 ERM (Exchange Rate Mechanism) 181, 188–9, 274
 sterling's membership of 193
 error-correction specifications/models 212–18
 conditional 264
 reduced-form vector 226
 serially uncorrelated 265
 error-correction terms 25, 84, 92
 absence of 59
 lagged 57
see also VECM
 errors 35, 71
 country-specific 63
 expectation 73
 forecast 155, 164, 168
 long-run 40, 46
 non-normal 199, 232, 266
 normally distributed 212
 orthogonalized 114
 reduced-form 88, 114, 115, 141, 265
 serially uncorrelated 107
 simulated 166–8
see also forecast error variance; structural errors
 ESRC (Economic and Social and Research Council) Macroeconomic Modelling Bureau 14 n.
 estimation 17, 29, 37, 41, 62, 63, 83
 biases in 56
 conditional 136, 168–9
 full information 4
 impulse response functions 231–48
 long-run 209–12
 long-run cointegrating vectors subject to identifying restrictions 124–7
 loss of efficiency in 56, 83
 probability forecasts 10
 reduced form system 59
 results and in-sample diagnostics 265–6
 stages of 198–200
 unrestricted 118
see also maximum likelihood estimation
 Euler equations 27, 73 n.
 stochastic 47
 euro area/eurozone 62, 212, 291, 293, 297
 modelling issues that arise from creation of 294
 shock effects 292, 295
 trend output 298
 European Community 34
 Evans, C. 51, 52, 53, 54
 Evans, C. L. 242, 245, 251 n.
 Evans, G. 248 n.
 event probability forecasts 280–5, 294
 exchange rates 187–9
 determined 64
 effective 71
 expectations 73, 75
 relating prices and output to 65
 unanticipated movements 99
 unexpected changes 90, 228
see also appreciation; depreciation; nominal exchange rate; real exchange rate
 exogenous variables 62, 109, 117, 135, 137, 138
 change in 15, 84
 common global 64
 deterministic and stationary 132 n.
 distinction between endogenous and 4, 49, 56, 169
 dynamic processes driving 139
 effect of a shock to 116
 foreign 293, 294
 influence of processes driving 139
 interactions between endogenous and 139
 number and list to be included 108
 restrictions on the processes generating 139
 shock effect measured to 110
 system long-run effects of 107
 unanticipated movements in 58
see also weakly exogenous variables
 expectations 39, 60, 75
a priori 205
 conditional 113, 230
 forward-looking 30
see also rational expectations
 expectations formation 14, 28, 92
 explanatory power 212, 218

exports 79, 80
demand for 290
expenditures on 75

Fabiani, S. 68
Fair, R. C. 13, 146
false alarm rate 271 n.
Favero, C. 23
Fed (US Federal Reserve Board) 4, 52, 54, 189–92
actions in federal funds market 53
evolution and development of macroeconomic modelling 14 n.
first and second generation models developed 13
feedback rule 93
Feldstein, M. 100 n.
Fernandez, C. 161
financial distress 305–6
financial markets 91 n.
globalisation of 62
very detailed knowledge of 54
financial sector 89
FIP (Fisher Inflation/Interest Parity) 65, 71, 73, 77, 102, 172, 211, 212, 242, 290, 291, 292
convergence to 233, 236
long-run 223
no economic rationale for including time trends in 207
firms 23
decision problems 20, 147
intertemporal optimisation problems 20
monopolistically competitive 22
optimising decisions 5
profit-maximising 14
first-order conditions 47, 93, 126
Euler 27
log-linearised 45
non-linear 44
fiscal policy 45
Fisher, P. G. 15 n., 211
forcing variables:
long-run 57, 61, 83, 130 n., 204
unobserved 112
forecast error variance 219
decomposition 115, 133, 134
forecast-inflation targeting 95, 98–9
forecast uncertainties 10, 109, 145, 149, 152, 153–61, 162, 163, 266–9
underestimated 169
forecasts 9, 29, 83, 84
conditional 94, 112

consistent with target 94–5
disaggregated 25
error variance of 114
global 15
multi-step 65
particularly useful method for presenting 10
potential ability of model 218
VARs primarily used for 4
world economy variables 63
see also probability forecasts
foreign assets 74, 77
demand for 76, 78, 79, 80
nominal interest rate paid on 73
revaluation of 75
foreign exchange markets 263 n.
foreign interest rates 8, 83, 189–93
effects of shock on 239–41
measured 259
positive differential of domestic over 245, 247
unanticipated movements in 99
unchanged on impact 242
unexpected changes in 90, 228
foreign output 8, 65, 83, 102, 172, 173–8, 236–9
co-movement between transitory components of UK and 258
decline 234
impulse responses 231, 244
foreign variables 8, 56, 57
country-specific 63
region-specific 64
separate measures of 63
forward-looking behaviour 42
France 172, 290, 293
Froot, K. A. 210 n.
Fuller, W. A. 106, 122, 200
functional form 212, 266, 300
misspecification 199
fundamental representation 17

Gali, J. 6, 18, 23, 42, 50–1, 54, 245 n.
GARCH error terms 177 n.
Garratt, A. 18, 54, 161, 177 n., 222, 264 n., 297
see also GRW
Gauss 10–11, 116, 112, 122, 233 n.
GDP (gross domestic product) 52, 68, 171, 172, 255
GDP deflator 52, 290
general equilibrium model 14, 20
explicit intertemporal 5

Germany 293
falling equity markets 295
interest rates 172
monetary unification (1990) 192
real output fall 296
Gerrard, W. J. 129 n.
Gertler, M. 23, 52
Giannone, D. 30
Gilchrist, S. 52
GIRF (Generalised Impulse Response Function) 8, 26–7, 112–14, 115–16, 132, 133, 139, 226, 231, 236, 239, 246, 248, 261 n.
global linkages 15
Godfrey, L. G. 129 n.
Goffe, W. L. 141 n., 208 n.
Gonzalo, J. 54, 55, 140 n., 248 n.
Gordon, D. B. 53, 54, 89 n., 93 n.
government agencies 25
government expenditure 42, 43, 75
Granger, C. W. J. 3, 57, 105, 106, 136, 146, 159, 160, 248 n., 269 n., 271
Granger, G. 3, 14, 106, 118 n.
Granger-causality 57, 118, 136
Granger non-causality 84
Greece 290
Griliches, Z. 37
Grilli, V. 210
GRW (Garrett-Robertson-Wright)
decomposition 248, 249, 255, 257–8
computation of 252–4
relationship of BN and 250–2
Gunther, T. A. 270, 272
GVAR (global vector autoregressive) models 62–5, 289, 292, 293, 294, 296, 297, 307
dynamic properties of 295–7
extending and updating 293

Hahn, J. 272 n.
Haldrup, N. 117 n., 203, 222
Hall, P. 167
Hall, S. 303
Hamilton, J. D. 17 n., 105 n., 204 n.
Hansen, G. D. 22
Hansen, L. P. 17 n., 47
Harding, D. 275
Harris, I. R. 156
Harvey, A. C. 249 n.
Harvey, D. I. 159
HBS (Harrod-Balassa-Samuelson) effect 71, 72
Heath Administration (UK) 181
Hecq, A. 248 n.
Hendry, D. F. 160 n., 266

Hercowitz, Z. 22
heterogeneity 5
information 22
heteroskedasticity 71, 129, 199, 212, 266, 300
HICP (Harmonised Index of Consumer Prices), *see* CPI
hit rate 271 n., 273
HMT (HM Treasury) 4, 14, 15 n.
Hodrick, R. J., *see* HP filter
Hoeting, J. A. 158, 161
Hong Kong 290
households 23
consumption expenditure 304
decision problems 20, 147
intertemporal optimisation problems 20
optimising decisions/behaviour 5, 22
utility-maximising 14, 43
see also representative household
HP (Hodrick-Prescott) filter 30, 101, 249, 257, 258, 259, 261
Huizinga, J. 210
Hurn, A. S. 140 n.
hypothesis testing 85
hysteresis effects 69 n.

identification 4, 14, 19, 27, 100
a priori 133
based on information flows 53
classical problem 109–10
contemporaneous relationships 87
explicit 28
implicit assumption 115
recursive approach 55, 115
short-run dynamics 48–51, 59
structural parameters, resolution of 110
identifying restrictions 18, 41, 54, 59, 87, 110, 113
estimation of long-run cointegrating vectors subject to estimation of 124–7
exact 118, 229
robust short-run 115
see also over-identifying restrictions
IMF (International Monetary Fund):
loan negotiations with 193
MULTIMOD multi-regional model 15
Special Drawing Right 172
imports 79, 80
expenditures on 75
impulse response analysis 110–16, 139, 294
cointegrating VARs 132–5
empirically coherent solution to 26
monthly model 300–3
surge of interest in the use of 297

impulse response functions:
empirical distribution of 141–3
estimates of 231–48
orthogonalised 134
see also GIRF; persistence profiles
impulse responses 16, 19, 25, 48, 87, 200,
225–61
long-run 18, 38
matching 30 n.
orthogonalised 17, 18, 49, 114–16
Inada conditions 69
income:
future, expected 76
nominal 76
private sector disposable 75
real money balances relative to 193–5
incomes policy 181
India 290
industrial action 177 n.
inference 63, 136, 139
inflation 3, 65, 90, 235
cointegrating relationship between
interest rates and 212
cost of deviations of 96
describing welfare in terms of 22–3
disequilibria between interest rates and
82
disequilibrium effects of money markets
on 292 n.
effects of oil prices on 183
expected 22, 72, 77
falling 240
high and low 182, 187, 193, 194
interest rate shock on 240–1
limited degree of positive co-movement
between output and 256
link between wage setting, minimum
wages and 290
long-run relationship between nominal
interest rates and 102
measuring 172
non-zero 100
price 178, 181
probability forecasts of 263 n., 274–85
rising 189
short-term trade-off between output
growth and reduction in 93
UK and world 183
wage 181
inflation targets 92, 94–7, 98–103, 181,
281–2
Bank of England 8, 10, 98
set explicitly 274
information disparities 71

information flows 54
exact timing of 227
identification based on 53
transitory impediments to 101
information imperfections 245
innovations:
correlation between permanent and
transitory 248
monetary policy 53
orthogonalised 17
policy 8
price-setting 50
random 208
short-term interest rates 91 n.
structural 50, 94, 99, 226
technological 211
instrument rules 94, 99
intercepts 108, 116, 210
restricted 121, 137, 138
unrestricted 121–2, 124, 138, 204
interest groups 25
interest rate changes:
foreign, unexpected 90
institutional and political costs of 93
interest rates:
assumption that UK rate has
contemporaneous impact on 229
cointegrating relationship between
inflation and 212
disequilibria between inflation and 82
effects of shock to 26–7
intertemporal links between prices, asset
returns and 67
long-term 53
market, monetary authorities try to
influence 89
negative effect on real money balances
211
oil price shock impact on 236
orthogonalised functions 26
setting 53
short-term 91 n., 294
unexpected increase in 242
unit shift in 26
volatility of 177
see also base rate; foreign interest rates;
nominal interest rates; real interest
rates
international trade 60
intertemporal optimisation 28, 67
attempt to integrate 38
dynamic decisions 3
explicit problem involving adjustment
costs 46

stochastic techniques 20
supplementing ‘intrinsic dynamics’
generated by 42
interval forecasts 146, 147, 154, 156
inventory models 47
'invertible' processes 17
investment 42, 46, 75
Iranian Revolution (1979) 183
Iraq 187
Ireland, P. 29
IRP (Interest Rate Parity) 73, 74, 77, 207,
210, 222, 292
convergence to 233, 236
IS (investment-savings) curve 22, 42, 50
Italy 293

Jacobs, J. P. A. M. 291, 292
Jaeger, A. 249 n.
Janssen, N. 193
Japan 290, 293, 293
falling equity markets 295
interest rates 172
output 296
Jeon, Y. 160
Johansen, S. 3, 36–7, 72 n., 83, 85, 105, 106,
122, 124, 125, 127, 136, 137 n., 204–5,
233 n., 266
Jørgensen, D. 37
Juselius, K. 72 n., 83, 233 n.

Kaminsky, G. 210
Kapetanios, G. 29
Kasa, K. 22
Keating, J. W. 54
Keynesian models 21, 50
see also New Keynesian DSGE models
Kilian, L. 204
Kim, K. 5 n., 7 n., 20 n., 22, 42, 46
Kim, S. 53
King, M. 98, 100
King, R. G. 6, 22
Klein, L. R. 13, 15, 307
Kolmogorov-Smirnov statistic 273
Koop, G. 26, 112, 229
Kuipers score 269, 270, 271, 272, 273
Kullback-Leibler information-theory 157
Kuwait 187
Kydland, F. 5, 22

labour 42, 68
steady-state inputs 44
labour market 60
changes in 69
models of 25

La Cour, L. 211–12
lag orders 108, 137, 198
determining 109
lag polynomials 148
Lagrange multipliers 125
Lagrangian function 44, 125
Lai, K. S. 205
large-scale models 4, 20–1
relatively poor forecasting performance of
14
scepticism concerning the use of 3
VAR models as benchmarks for evaluation
of 18
Lastrapes, W. D. 54
Latin America 293, 295, 296
'Lawson boom' 177
LBS (London Business School) 13, 15 n.
learning 42
incomplete 73 n.
least squares 4
see also OLS
Lee, K. C. 116, 177 n., 211 n., 233 n., 298,
303, 304, 305
Leeper, E. M. 53, 54, 89 n.
LeRoy, S. 49
Levtchenkova, S. 19 n.
Levy, M. S. 157
likelihood 8, 146, 208 n.
predictive 156, 162
Lin, J. L. 57, 136
liquidity 78
price of 89 n.
liquidity effects 292 n.
sizeable 243
strong 236
liquidity trap 100
Litterman, R. 4, 18, 22
log-likelihood 125, 128
maximised 108
log-likelihood ratio statistics 123, 128, 140,
141, 208, 299
Long, J. B. 5
long-run disturbances 82, 83, 102
reduced-form 57, 58, 101, 226
structural 226 n.
long-run modelling approach 6–9
long-run multiplier matrix 135, 136
long-run relationships 5, 6, 23, 30, 233,
266, 290
deviations from 26
economic theory of 67–85
empirical validation of 28
ensured existence of 107
equilibrium 39

long-run relationships (*cont.*)
 identification of 18, 36–7, 54–5, 39, 61
 nominal interest rates and inflation 102
 structural 7, 14, 24, 26, 46, 197–223
 varying speeds of adjustments of 239
 Lopez, J. A. 159
 loss function:
 difficulty of formalising 109
 explicit 109
 Lothian, J. R. 210
 LQ (linear-quadratic) models 146, 147
 general equilibrium 47
 optimisation 38, 89
 Lucas, R. E. 3, 14
 Lütkepohl, H. 131 n., 219

McAleer, M. 105 n.
 MacDonald, R. 210 n., 211, 212
 MacKinnon, J. G. 138 n.
 major world economies 15, 16
 Mankiw, N. G. 211
 marginal models 58, 59, 139
 Mark, N. C. 210 n.
 market failures 21
 market forces 67
 market uncertainties 28, 67
 Markov chain model 158 n.
 Marshall, D. 22
 martingale property 250, 252
 Mauro, F. di 62, 292, 293–4, 299
 Mauskopf, E. 13
 maximum likelihood estimation 59, 85, 88,
 105, 106, 122, 123, 124, 126, 128, 137,
 138, 141 n., 142, 143, 157, 166, 199, 254
 constrained 125
 exactly identified 125
 medium-size economies 293
 Medium Term Financial Strategy (UK 1979)
 188
 Mellander, E. A. 6
Microfit 10, 127, 233 n.
 Middle East 293, 294 n., 296
 Mihov, I. 52, 53
 Mills, T. 68
 miners strike (UK 1971) 177 n., 212
 Minnesota priors 18
 Mishkin, F. S. 211
 Mitchell, J. 298, 303
 Mizen, P. 303, 304, 305
 MME (money market equilibrium condition) 207, 211, 222, 242
 convergence to 233, 236

effect of monetary policy shock most
 pronounced 242
 model selection criteria 85
 Modigliani, F. 13
 Monacelli, T. 23 n., 42, 245 n.
 monetary policy:
 contractionary 189
 credibility of 93 n.
 impact of 22, 291
 implications for analysis 23
 instrument rules and target rules in
 guiding 94
 investigating the effects of 6
 measuring the effects of 51–4
 modelling 89–97
 motivation for current arrangements in
 UK 146
 non-accommodating 192
 policy-makers encouraged to consider
 output consequences of 100
 potential role in generating economic
 fluctuations 21
 rules 5
 shocks effects in G7 economies 298
 should aim at price level targeting 100
 significant impact on conduct of 232
 ‘super-non-neutrality’ of 78 n.
 systematic component of 91
 tightening of 233, 236, 243
 transmission mechanisms 290
 monetary policy shocks 8, 26, 51, 53, 91,
 97, 225
 assumed to satisfy standard orthogonality
 condition 92
 contemporaneous dependence of 233
 contractionary 242, 245
 economically meaningful 227, 242
 effects of 242–8
 identification of 27, 33, 38, 54, 87, 89, 98,
 99, 102, 227–31
 monetary union 62
see also EMU
 money 22
 high-powered 76, 77
 role of 67
see also real money balances
 money demand 50, 100, 207, 255, 291, 299
 money markets 212
 possible disequilibrium effects of 292 n.
 very detailed knowledge of 54
see also MME
 money stock 172
 money supply 50, 51, 53, 298
 excess 243

money velocity 207, 211
 real narrow 193
 Monte Carlo techniques 105 n., 123, 160 n.,
 161
 Morgan (J.P.) 623 n.
 Morley, J. C. 249 n., 252
 Motto, R. 298
 moving-average representation 55
 final form 114
 infinite 111, 118
 level 120, 132
 unique 17
see also ARMA
 MPC (UK Monetary Policy Committee) 274
 multivariate models 252
 multivariate normal densities 230
 multivariate normal distribution 141, 208
 Murphy, C. W. 13, 15 n.
 Murphy, P. D. 211
 Muscatelli, V. A. 140 n.

Nason, J. M. 22
 Neave, H. R. 273 n.
 Nelson, C. R. 3, 68, 106
see also BN decomposition
 neoclassical growth model 70, 72
 Nerlove, M. 37
 New Keynesian DSGE models 5, 20 n., 22,
 23 n., 28, 38, 42
 New Zealand 290
 Newbold, P. 3, 105, 159
 Newton-Raphson algorithm 127, 208 n.
 Ng, S. 54, 55, 248 n.
 Nickell, S. 46, 48 n., 69 n.
 NIESR National Institute of
 Macroeconometric Modelling Economic
 and Social Research) 13–14
 NIGEM (National Institute Global
 Econometric Model) 15
 Nixon administration (US) 189
 nominal exchange rate 293
 current account balance reaction to
 changes 15 n.
 effective 171
 foreign, generally falling 192
 impact effect of monetary policy shock on
 245
 small appreciation of 235
 nominal interest rates 22, 72, 73, 77, 78, 223
 foreign 172
 high 193
 long-run relationship between inflation
 and 102

short-term 65
 zero bound to 100
 nominal rigidities 5
 non-parametric bootstrap 208
 non-tariff barriers 71
 normalisation conditions 36, 70, 110, 130,
 207
 normality 129
 chi-squared statistics for 232
 null hypothesis 3, 106, 123, 272

objective function 47, 95, 98, 100
 central role in short-run economic theory
 99

observed variables 26, 50
 balance struck between integration
 properties and desired target values 101
 contemporaneously 52
 effects of shocks to 27
 long-run equilibrium relationships and 39
 Obstfeld, M. 71 n.
 OECD countries 171, 172
 common model structure across 15
 output 173, 211

oil price shocks 89–90, 175, 188, 192, 227
 effects of 183, 232–6
 impulse responses arising from 301
 impulse responses to 231
 role in worldwide productivity slowdown
 72 n.
 uncorrelated 84

oil prices 8, 64, 83, 87, 227, 268
 average crude 172
 changes in 92, 197
 determined 90
 effects to 26, 197, 223
 evolution of 84
 fall in 183–7, 188
 hikes in 183, 212, 300
 innovations 8
 international 56
 long-run forcing 88, 233, 264
 relative 72
 rises 177, 181, 188, 232, 236
 unanticipated movements in 99
 weakly exogenous 231

Okun, A. 50, 100
 OLS (Ordinary Least Squares) 88, 128, 129,
 138, 155

OPEC (Organization of Petroleum-Exporting
 Countries) 192

open economies 20, 42
 small 26, 56, 67, 70, 83, 245 n., 293

optimisation 5, 44, 208 n.
 quadratic 47
see also intertemporal optimisation
 optimisation problems 92–3, 99
 orthogonalisation 17
 apparent atheoretic content of 49
 output 4, 42, 90
 aggregate 68
 contemporaneous 50, 51, 52
 describing welfare in terms of 22–3
 desired 100, 101
 determination of 68–70, 101
 effects of shock to 26
 exchange rates and 65
 expected real interest rate and 22
 falls in 232, 233, 239
 inflation and 22, 256
 news likely to impact on 56
 nominal 78
 pairwise approach to testing for 121
 possible disequilibrium effects of money markets on 292 n.
 potential 39, 100, 101, 102
see also foreign output
 output gap 100, 101, 207, 211, 222, 233, 236, 242, 292
 measures of 298
 output growth:
 bivariate VAR model of 19
 fixed target level for 96
 probability forecasts of 263 n., 274–85
 short-term trade-off between inflation reduction and 93
 over-identifying restrictions 41, 106, 110, 124, 125, 141, 208, 299
 asymptotic critical values of 199 n.
 long-run 138
 testing the validity of 127–9, 140
 tests of 199
 theory-based 207
 validity of 268
 overshooting model 245
 Oxley, L. 105 n.

Pagan, A. R. 5 n., 7 n., 17, 20 n., 22, 42, 46, 55, 243 n., 275
 Palm, F. C. 248 n.
 parametric approach 167
 Pareto optimal outcomes 21
 permanent-transitory decomposition 298
 Perng, S. K. 157
 Perrier, P. 29 n.
 Perron, P. 72 n.
see also Phillips-Perron test

Persian Gulf War (1990) 187
 persistence profiles 27, 116, 135, 200, 232, 233, 242, 245
 empirical distribution of 141–3
 main attraction of 134
 scaled 134
 Pesaran, B. 10, 127, 233 n.
 Pesaran, M. H. 10, 15, 16 n., 20 n., 25, 26, 27, 29, 35 n., 37, 41, 42, 45, 47, 48 n., 55, 59, 63 n., 69, 70, 83, 84 n., 85, 89, 105, 107, 109, 112, 116, 118, 121, 122, 123, 124, 126 n., 127, 128, 129, 134, 135, 137 n., 138 n., 146, 158, 161, 177 n., 199, 203 n., 205 n., 211 n., 225 n., 230, 232, 233 n., 292, 297, 298, 299
see also PSW; PT statistic
 Pettenuzzo, D. 158, 203 n.
 Phillips, P. C. B. 3, 37, 105, 124, 200
 Phillips curve 22, 42, 50
 backward-and-forward-looking effects in 23
 Phillips-Perron test 200–1, 222
 Plosser, C. I. 3, 5, 21, 68, 106
 point forecasts 146, 147, 148, 154, 155, 178, 275–8, 296
 pooled 159–61
 policy analysis 15, 109
 policy evaluation 14
 policy rule 42
 Portfolio Balance Approach 76
 positive definite matrices 84, 165, 265
 Poulicac, D. 263 n.
 power utility function 20
 PPP (Purchasing Power Parity) 71, 72, 74, 79, 81, 172, 203, 242, 290
 absence of trend in 207
 deviations from 233
 investigating, using cointegration analysis 210
 restored 236
 small deviation from 292
 prediction density 157
 predictions 158 n.
 long-run 84, 197
 tested 42
 uncertainties on 156
 preferences:
 monetary authorities 93, 94, 97, 99
 well-behaved 73 n.
 prequential approach 146
 Prescott, E. C. 5, 22
see also HP filter
 pre-test bias 108

price indices 72
 producer 172
see also CPI; RPI
 price rigidities 22, 68
 price-setting 50
 arbitrary nominal rigidities in 21, 23
 prices 65, 67
 asset 294 n.
 commodity 51, 52, 53
 common currency 71
 determination of 203
 foreign 8, 178–87, 203
 producer 171
 relative 72, 80, 235
 reset periodically and with fixed probability 23
 retail 171
 shadow 45
 upward pressure on 181
see also oil prices
 pricing behaviour 22
 priors 18
 non-informative 155, 156, 157
 vague 197
 private sector behaviour 101
 probability density function 157, 158
 probability distribution function 116, 162
 non-degenerate 69
 predictive 165, 166
 time-invariant 70
 probability distributions 20
 prior 109
 steady-state 69
 probability forecasts 2–3, 8, 145–69, 200, 219, 263–88
 interpretation of 10, 178
 measuring financial distress 303–6
 usefulness of 10
 production constraint 43
 production technology 68–70
 productivity differentials 70
 productivity:
 relatively rapid growth 71
 worldwide slowdown in 72 n.
 profit maximisation 70
 Proietti, T. 248 n.
 PSW (Pesaran-Schuermann-Weiner) 62, 64, 172 n., 293, 294, 295, 296
 PT (Pesaran-Timmermann) statistic 269, 271, 272, 273
 quadratic equations 46
 quadratic trends 120
 Quah, D. 4, 18, 19, 54, 55

random variables 116
 independently and identically distributed 147
 probability distribution function of 116
 time-invariant 69
 random walks 105, 264, 268, 271
 martingale property shared by 250
 with drift 43, 232
 rational expectations 35 n.
 advent of 14
 explicit reliance on 42
 identification of 3 n.
 log-linear system of 20
 multivariate linear 45
 restrictions implied by 38
see also REH
 RBC (Real Business Cycle) 5, 18, 21, 28
 short-run restrictions involved in 38
 reaction functions 93, 94–7
 Reagan administration (US) 192
 real equity price index 293
 real exchange rate 72, 81, 293
 evidence of a unit root in 210
 stationarity of 79
 real factors 5
 real interest rates 73
 average 103 n.
 expected, relating output to 22
 long-run level 102
 real money balances 290, 293
 elasticity of 211
 oil price shock affects 236
 relative to income 193–5
 strong negative effect of interest rates on 241
 real rates of return 73
 annual 211
 expected 72, 77
 steady-state distribution 70
 recession 3, 264, 305
 avoiding 8, 275
 growth prospects and 282–5
 probability of 306
 recursive structure 38, 48, 49
 block 51, 53, 59, 60, 61
 imposing 49, 51
 regional interdependencies 292–7
 regressions 48, 109, 138, 156, 211
 error-correcting 57, 199
 finite-order 131 n.
 linear 157

regressions (*cont.*)
 spurious 3, 105, 106
see also OLS
 regularity conditions 46, 157
 mild 69
 REH (Rational Expectations Hypothesis) 73 n.
 Reichlin, L. 248 n., 251 n.
 rejection level 209
 representative agent paradigm 20
 representative household 42
 forces outside the control of 43
 Social Planner maximises utility 43
 reserves 51–2, 53
 residuals 141, 167
 estimated 208
 non-normality in 205, 208
 reduced-form 229
 serially uncorrelated 232
 transformed 168
 restrictions 49, 55, 88, 89
a priori 82, 110, 114, 227
 co-trending 120, 121
 economic importance of 109
 evidence to support validity of 209
 exactly identifying 208
 exclusion 51
 imposed through tentative theory 49–50
 ‘incredible’ 3
 just-identifying 141
 long-run 6, 138, 255, 259
 normalisation 110
 rank 118
 short-run 38, 59, 87, 227
 system dynamics 46
 theory-based 298
see also covariance restrictions; identifying restrictions; over-identifying restrictions
 returns to scale 68
 Ribba, A. 298
 ‘rice puzzle’ 245
 Ríos-Rull, J. 22
 risk-averse agents 72, 73
 risk premia 72, 73
 deterministic component of 210
 secondary effects of shock on 245
 Robertson, D., *see* GRW
 Robertson, J. C. 243 n.
 Rogoff, K. 71 n., 93 n., 210 n., 233 n.
 Rosenblatt, M. 272
 Rotemberg, J. 52
 Roubini, N. 53

Rovelli, R. 23
 RPI (Retail Price Index) 172, 181, 274, 276 n.
 Sachs, J. 72 n.
 Sala-i-Martin, X. 69, 233
 Sampson, M. 22
 Sargan, J. D. 106
 Sargent, T. J. 17 n., 47, 266 n.
 satellite models 25, 59–62, 289, 303–5
 Saudi Arabia 187
 SBC (Schwarz Bayesian Criterion) 85, 108, 163, 198, 204, 218, 219, 221, 268, 269, 270
 Schorfheide, M. 23, 28
 Schuermann, T. 15, 16 n., 292, 297
see also PSW
 Schumacher, C. 298
 Schwarz, G. *see* SBC
 SDR (IMF Special Drawing Right) 172
 sectoral models 59–62
 selection matrix 253
 Selgin, G. 54
 SEMs (simultaneous equation models):
 emerging consensus between 292
 forward-looking models of form
 associated with 35 n.
 large-scale 13–16, 20, 24–31, 291
 structural 230
 sensitivity analysis 109
 sequential conditioning decomposition 168
 sequential procedures 108
 serial correlation 218
 chi-squared statistics for 232
 residual 129, 199, 212, 266
 residual 300
 shadow prices 45
 Shin, Y. 26, 27, 29, 37, 41, 59, 83, 84 n., 85, 89, 105, 107, 109, 112, 116 n., 118, 122, 123, 124, 126 n., 127, 128, 129, 134, 135, 137 n., 138 n., 199, 205 n., 230, 232, 233 n.
 shock effects 26, 114, 183, 232–48, 295
 contemporaneous, restrictions on 18
 decomposition of 298
 dynamic 33
 financial markets on business cycles 62
 foreign 292
 identification of 89
 measured 33, 110–11
 permanent 4, 8
 persistent 35
 system-wide 27, 134
 temporary 4, 133

shock responses 21
 accumulated 15
 dynamic 8, 16
 impulse 225, 226, 227, 229
 long-run 54
 short-run 8
 shocks 17, 28, 112, 139
 adjustments to 233
 contractionary 301
 demand/supply 4, 19, 26, 50, 54–5, 89, 257, 298
 dynamic impact of 225
 economically meaningful 10, 33, 36, 61, 298
 estimated 48
 euro area economies and impact on UK 62
 exogenous 34, 45
 future 149
 generated in stochastic simulation 166
 identification of 54, 89
 non-zero contemporaneous dependence of 64
 observed correlation of 141
 orthogonalised 49, 54
 output 51, 236–9
 predicted 113
 productivity 5, 50, 51, 72
 real 21, 72
 reduced-form 25, 115, 226, 227
 restrictions on 4, 19
 stationary 19
 system-wide 116, 134
 technology 20, 89
 tracking 29
 white-noise 19
see also monetary policy shocks; oil price shocks; structural shocks
 short-run dynamics 21, 25, 28, 33, 37, 84, 212
 captured more accurately 204
 identification based on tentative theory on contemporaneous relations 48–51
 imposing structure on 38
 impulse responses based on 30 n.
 restrictions on 3, 38, 110
 unconstrained 219
 short-run economic theory 87–103
 short-run relationships 39
 short-run response matrices 135
 signal extraction and learning 22
 Sims, C. 3, 4, 8, 14, 15, 16, 17, 18, 37, 38, 40, 48, 49, 52, 55, 91 n., 110, 114, 226
 simulated annealing routine 141 n., 208 n.

simulation 209
 stochastic 156, 162, 164–6, 269
 Skouris, S. 269 n.
 Smets, F. 5 n., 20 n., 23, 303
 Smith, J. 160 n.
 Smith, L. V. 62, 292, 293–4, 299
 Smith, R. J. 29, 41, 59, 84 n., 85, 105, 107, 118, 122, 123, 135, 137 n., 138 n., 199, 205 n.
 Smith, R. P. 14 n., 20 n., 25, 42 n., 62, 225 n., 230 n., 292
 Smith, V. 62, 225 n., 292
 Social Planner 43–4
 Solow model framework 69 n., 101
 solvency:
 institutional 67
 key conditions 6
 long-run 23, 75–81
 South East Asia 293, 295, 296
Special Issue of the Journal of Economic Surveys 105 n.
 speculative behaviour 245
 speculative effects 73
 stability condition/assumption 107, 110
 Stadler, G. W. 22
 stagflation 14
 standard deviation 112, 177, 239
 standard errors 232, 233, 242
 asymptotic 210
 state of emergency 177 n.
 stationarity 17
 stationary processes 73, 76, 80
 normalised 70
 statistical significance 17, 57, 109, 212
 steady-state properties:
 clearly defined 42
 non-linear equations illustrate 44
 steady-state relationships 81
 long-run, derivation of 67
 steady-state solution 24
 steady-state values 46, 68
 non-stochastic 44, 45
 sterling 187, 188–9
 sticky price models 38
 stochastic process 29
 break point 158 n.
 stochastic simulations 156, 162, 164–6
 Stock, J. H. 248 n., 251 n
 stock-flow:
 constraints 27–8
 equilibria 67, 80
 identities 23
 relationships 74–5

- stock market crash (1987) 192, 212
 Strachan, R. W. 292
 Strongin, S. 53
 structural coefficients 36, 231
 contemporaneous 34, 88, 227
 exact identification of 37, 88
 identification of 111, 113
 unknown 34
 structural cointegrating VAR approach 5, 7, 13, 16 n., 23–31, 33
 investigating 297
 recent applications of 289–92
 structural errors 54, 58, 59, 133, 135
 a priori restrictions on covariance matrix of 18
 indeterminacy confined to
 contemporaneous interaction of 114
 long-run 26
 orthogonal 113
 shock to 110, 111, 112, 113, 133, 231
 structural shocks 35, 41, 226
 composite shock generated by 95
 contemporaneous dependence between 58
 covariance assumed to be diagonal 19
 economically meaningful 36, 39
 effects of 99, 115
 identification of 37–9, 50, 89
 independent of each other 48
 long-run 23
 orthogonalised 18–19, 55
 permanent 55
 serially uncorrelated 88, 227
 timing of reactions of various variables to 25
 transitory 55
 unpredictable 96
 structural VAR approach 4, 18, 18–19, 25–7, 38, 48, 54, 115
 see also structural cointegrating VAR
 structural VARX model 106, 107, 107–9, 115
 long-run 105
 Summers, L. 100
 supply:
 excess 39
 labour 68, 69
 reserves 53
 shocks effect on output 54–5
 Svensson, L. E. O. 92 n., 93 n., 94, 95, 96 n., 100
 Sweden 6 n., 28 n., 292
 target rules 94, 99
 tariff barriers 71
 tastes 20, 28
 shocks to 225
 tatonnement process 39
 taxation 69
 Tay, A. S. 270, 272
 Taylor, J. B. 103 n.
 Taylor, L. W. 129 n.
 Taylor, M. P. 210
 Taylor, R. 177 n.
 technological change 28
 technological progress:
 characterising 38
 economy determined by level in rest of world 70
 endogenous 5, 22
 foreign 70
 labour augmenting 44, 68
 simple model of 101
 steady-state growth path of variables driven by 44
 underlying common measure of 102
 technology:
 constraints 14
 exogenous shock to 45
 government expenditure expressed relative to 43
 payments technology 193
 production 68–70
 shocks to 225
 tentative economic theory 38, 53, 54–5, 87, 89, 115
 contemporaneous relations 48–51
 term premium:
 determined by unanticipated factors 89–90
 expected, time-varying 92
 predictable component of 91
 terms of trade 188
 test statistics 140–1
 Thai economy 291
 Thatcher administration (UK) 188
 time endowment 42
 time series 3, 24, 166, 193
 containing unit roots 105, 106
 limited data available 268
 univariate models 221
 Timmermann, A. 158, 203 n.
 see also PT statistic
 Tinbergen, J. 13
 Tinsley, P. 13
 TOTEM model 29 n.
 trade balance relationship 81

- Trade Unions 181
 transactions costs 73
 rigidities that arise from 26
 transparency 146
 transport costs 71
 transversality conditions 20
 Treasury Bills 54, 171
 trend coefficients 7, 85, 108, 147
 restricted 120, 136, 204, 207, 250
 trend/cycle properties 225–61
 trend-stationary models 147, 149–51
 Treutler, B. J. 292, 297
 trivariate models 210
 Turkey 290
 Turner, D. 15 n.
- UIP (Uncovered Interest Parity) 71, 73, 210, 211, 245
 uncertainties 8
 bond and foreign exchange 73
 money and goods market 72
 see also forecast uncertainties
 unconditional probability 178
 unemployment 4, 54
 bivariate VAR model of 19
 cyclical fluctuations 68
 determined solely by productivity shocks 50
 equilibrium 69
 fall in 177
 long-run equilibrium 68
 unique stable solution 46
 unit roots 3, 5, 46, 64, 68, 69, 70, 107, 123, 248
 probability forecasts 149, 151
 properties of core variables 200–4
 tests for 106, 122, 177 n.
 time series containing 105, 106
 VARs with 116
 United Kingdom 293, 295
 impulse response and trend/cycle properties 225–61
 long-run structural model 197–223
 macroeconomy 171–95
 possible effects of joining Euro area 292
 probability event forecasting 263–88
 probability forecasting and measuring financial distress 303–6
 real output fall 296
 United Nations Project Link 15, 307
 United States 212, 293, 297, 298
 budget deficit 189
 falling equity markets 295
 interest rates 172
 real output fall 296
 see also Fed
 univariate approaches 261
 univariate models 43, 147–53, 252
 benchmark, comparing core model with 218–21
 unrestricted VAR models 4, 7, 16–18, 19, 24, 25–7, 40, 84, 118, 197, 198
 log-linear 23
 small 264
 Urbain, J. 248 n.
 utility functions:
 underlying 28
 weight given to leisure in 43
 utility-maximising 14, 43–4
- Van Dijk, H. K. 292
 VAR (vector autoregressive) models 35, 40, 48, 50, 52 n., 55, 115, 268
 augmented 107–16
 bivariate 4, 19, 54, 55 n., 210
 computation of probability forecasts based on 164–6
 considerable interest in the use of 3
 finite order 17
 global 16 n., 293
 innovations in different variables in 114
 large dimensional 65
 models with weakly exogenous variables 57–9
 number of parameters estimated in 61
 restricted 5, 25
 stationary 116
 trend coefficients in 7, 85
 underlying 85, 172, 204, 236, 253
 see also cointegrating VAR; structural VAR; unrestricted VAR
 variables:
 cointegrated 116, 211
 contemporaneously determined 90, 92
 country-specific 64
 decision 47
 dependent 212
 deterministic 107, 108
 difference-stationary 40, 84
 discounted future 20
 expectational 92
 explanatory 60
 foreign 293, 294
 global 64
 instrumental 4
 long-run responses to shocks 54

- variables: (*cont.*)
motivation for long-run relationships
 between 75
non-stationarity in 3
not affected by disequilibria 56–7
predetermined 109, 110
quadratic trends in level of 118
sectoral 60
short-run evolution of 199
stationary 35, 115, 118
target 93, 94, 95, 98, 99, 101
unit root 3
see also core variables; endogenous
 variables; exogenous variables; forcing
 variables; foreign variables; observed
 variables
variance-covariance matrices 17, 58
 estimated 49
positive definite 35, 107, 227
reduced form errors with 36
VARMA (vector autoregressive moving
 average) models:
 estimation of 17
finite order process 17
infinite order 131
VARX (vector autoregressive exogenous)
 models 20, 31, 42, 113
cointegrating 6, 63
DSGE model fits readily into 46
large dimensioned 208
log-linear 5, 6
reduced form 109–10
unrestricted 6
see also structural VARX model
VAT (value-added tax) 181
VECM (vector error-correcting model) 30,
 34–5, 40, 106, 117, 120, 121, 197,
 209–21, 249, 293
adjustment costs models frequently
represented by 48
augmented autoregressive 105
conditional 128–9, 138
core 248
estimated 41, 49, 122, 128–9, 138,
 141
extended 135
full-system 138
individual country (or region)
 models 63
multivariate 259
reduced form 49, 92
structural 55, 88, 89, 137, 138, 226
triangular 37
underlying 254
Vietnam War 189
volatility 159, 177, 181, 187, 188,
 245 n., 303
- wage rigidities 22
 nominal 68
 real 68
wage setting 290
 arbitrary nominal rigidities in 21
wages:
 minimum 290
 zero increases 181
Wallis, K. F. 14 n., 15 n., 160 n., 263 n., 275
Wallis, K. W. 291, 292
Walrasian general equilibrium model 14, 21
Watson, M. 18
Watson, M. W. 105 n., 248 n., 249 n., 251 n.
weakly exogenous variables 25, 34 n., 63,
 64, 106, 169, 227
oil price 204
VAR models with 57–9
Weiner, S. M. 15, 16 n., 292, 297
see also PSW
Weiss, L. 22
welfare 101
 describing in terms of inflation and
 output 22–3
 reducing 21
West, K. D. 46–7
Western Europe 293
Whitley, J. D. 15 n., 25
Wickens, M. R. 20 n., 36 n., 298
Wilson Administration (UK) 181, 192
'Winter of Discontent' (UK 1978/79) 181
Wohar, M. E. 290
Wold-causal ordering 38
Wold decomposition theorem 16, 17 n.
Woodford, M. 52, 100 n., 101
Worthington, P. L. 273 n.
Wouters, R. 5 n., 20 n., 23
Wren-Lewis, S. 15 n.
Wright, S., *see* GRW
- Yom Kippur War (1973) 183
Yule, G. U. 3, 105

Zaffaroni, P. 161

Zha, T. 52

Zimbabwe 290