

# Discussion of “Understanding the Great Recession”

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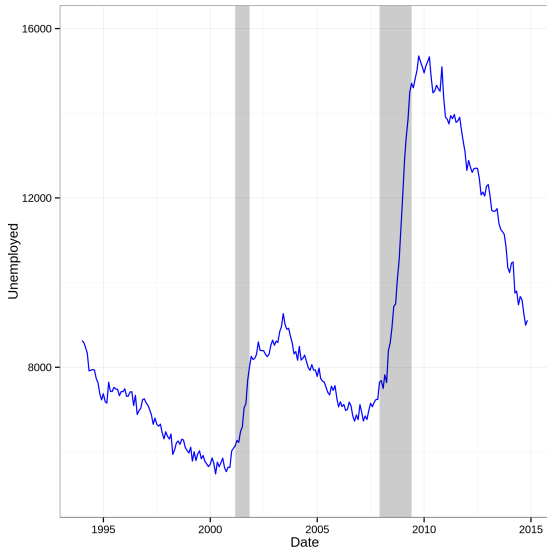
## The Paper

- Estimates a New-Keynesian model that allows the authors to uncover which types of adverse shocks were responsible for the dynamics of the 2008 recession.
- Nonlinearity introduced as a result of the ZLB.
- Labor markets take a prominent role.
  - Participation margin - home production.
  - Wage bargaining has Nash as special case (sluggish wages but no nominal wage rigidity).
- MP: Taylor rule with explicit ZLB constraint, forward guidance (2011-)

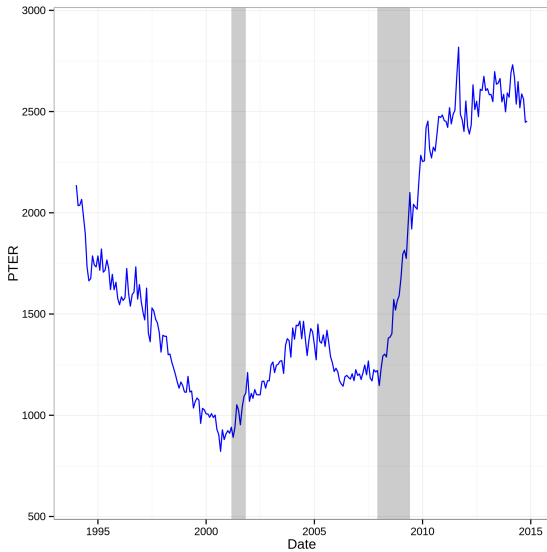
# The Paper

- **Finding:** Two shocks account for large drop in economic activity:
  - Shock to Euler eq. risk-free asset accumulation.
  - Shock to Euler eq. capital accumulation.
- Two additional shocks relevant for dynamics.
  - Shock to TFP.
  - Shock to fiscal policy.

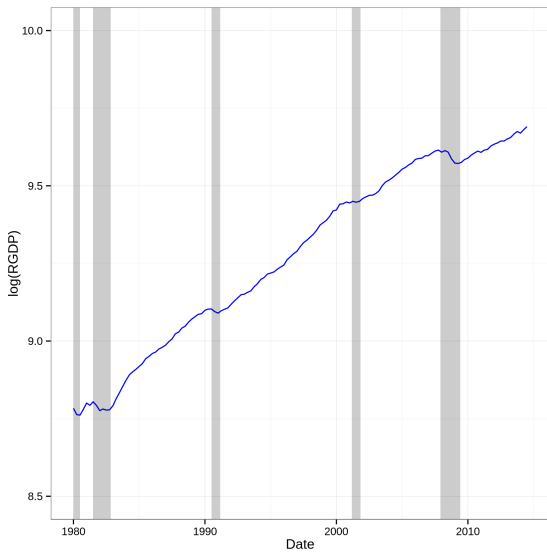
# Unemployment



# But They Can't Find FT Jobs



# Log-Output



# Wage Rigidity in Great Recession

$$\log(w_{i,k}) - \log(w_{i,k-s-1}) = \gamma X_{i,k} + \sum_{t=1}^T \phi_t \chi_{i,t} + \epsilon_{i,k}.$$

$$\phi_t = \alpha + \beta \Delta U_t + \nu_t,$$

# Wage Rigidity in Great Recession

Table: 1991, 2001, and 2008 Recessions

	1991	2001	2008
$\beta$	0.0005	0.021	<b>-0.046</b>



# Reallocation and Wage Changes in Great Recession

Table: Industry Transition and Wage Changes

	1991	2001	2008
Agriculture	-1.9	-1.1	-2.2
Manufact.	-3.5	-8.0	-9.9
Construct.	-1.7	-13.7	-18.8
Low-Skill Serv.	9.7	8.4	13.1
High-Skill Serv.	-0.3	-6.0	-5.6

## Finance, Labor, and MP

- Labor market turbulence  $\rightarrow$  large income shocks for (some) households.
- Drop in permanent income for (some) households affected.
- Tightening of credit constraints  $\rightarrow$  consumption and output dynamics (Lorenzoni and Guerrieri (2012), Huggett (1993))
- Does it matter for understanding GR?
- Does it matter for monetary policy? Conventional? Unconventional?

## Finance, Labor, and MP

- Not (yet) large literature on idiosyncratic, precautionary savings, incomplete markets and its relationship to MP.
- J. W. Lee (2014): more weight on price stability as financial frictions rise.
- A. McKay and R. Reis (2012): large transfer and taxes programs (e.g. large part of ARRA) matter for aggregate fluctuations.
- A. McKay, E. Nakamura, J. Steinsson (2014): precautionary savings diminish the power of forward guidance.
- Sheedy (2012): Rationale for NGDP targeting.

THANKS!