

Contents

<i>Preface</i>	vii
<i>About the Author</i>	xi
1 Introduction to Dynamic Macroeconometrics	1
1.1 Introduction	1
1.2 Cobweb Model Dynamics	3
1.3 Stable and Unstable Dynamics	6
1.4 Stationary State and Equilibrium Correction	8
1.5 Random Fluctuations	10
1.6 Estimation of Cobweb Model Dynamics	12
1.7 Business Cycle Dynamics	13
1.8 Causality, Correlation and Invariance	17
1.9 Overview of the Book	21
1.10 Questions and Answers and Statistical Software and Datasets	27
1.11 Exercises	27
2 Review of Econometric Theory	31
2.1 Introduction	31
2.2 Probability and Random Variables	32
2.3 Statistical Concepts for Modelling of Relationships	39
2.4 The Simple Regression Model	42
2.5 Estimation of a Structural Equation Between Two Variables by IV	55

2.6	Multivariate Regression and Structural Equations	61
2.7	Model Equations with Time Series Variables	82
2.8	Misspecification Testing	86
2.9	Recommended Textbooks in Econometrics and Mathematics for Economists	97
2.10	Exercises	99
3	Review of Difference Equations	103
3.1	Introduction	103
3.2	Deterministic Difference Equations	104
3.3	Stochastic Difference Equations with Constant Coefficients	107
3.4	The Companion Form	125
3.5	Difference Equations and Lag Operator Notation	129
3.6	Impulse-Responses and Dynamic Multipliers	136
3.7	Final Equation Form of a Multiple Equation System . .	140
3.8	Companion Form Representation of a System	143
3.9	Summary and Looking Ahead	145
3.10	Exercises	145
	Appendix 3.A Some Results for Complex Numbers	146
4	Stationary Time Series	157
4.1	Introduction	157
4.2	Time Series, Stochastic Processes and Difference Equations	158
4.3	Stationarity	162
4.4	Ergodicity	164
4.5	Stationary Time Series Variables	165
4.6	ML and OLS Estimation of the AR(1) Model	184
4.7	ML Estimation of the AR(p) Model	193
4.8	ML Estimation of ARMA Processes	194
4.9	Multiple Equation Processes	194
4.10	Summary and Looking Ahead	197
4.11	Exercises	197
	Appendix 4.A Preservation of Stationarity by Linear Filtering	198

5	The VAR	203
5.1	Introduction	203
5.2	Estimation of the VAR	204
5.3	A VAR Example (Cobweb Model Data)	209
5.4	VAR Impulse-Response Functions	215
5.5	Forecasting from VARs	217
5.6	Modelling Beyond the VAR	219
5.7	Exercises	220
6	Single Equation Models	221
6.1	Introduction	221
6.2	ADL Model Equations	222
6.3	Dynamic Multipliers of ADL Model Equations	231
6.4	Equilibrium Correction Model	238
6.5	Special Cases of the ADL Model	243
6.6	Geometric Lag Distribution	248
6.7	Empirical ADL Modelling of Interest Rate Transmission	249
6.8	Volatility Modelling	252
6.9	Exercises	253
7	Multiple Equation Models	257
7.1	Introduction	257
7.2	Extending the System: VAR-EX	258
7.3	Modelling the VAR by Conditional and Marginal Equations	259
7.4	Simultaneous Equation Model	261
7.5	Identification	262
7.6	Order and Rank Conditions	264
7.7	Recursive Model	267
7.8	Structural VAR	270
7.9	Estimation Methods for Structural Models	272
7.10	Model Equations with Rational Expectations	286
7.11	Future-Dependent Models	291
7.12	Exercises	295
	Appendix 7.A Algebra Showing 2SLS and GIV Equivalence	297

8	Exogeneity	301
8.1	Introduction	301
8.2	Weak Exogeneity	302
8.3	Granger Causality and Strong Exogeneity	304
8.4	Parameter Invariance and Super Exogeneity	305
8.5	Exogeneity Tests	307
8.6	Exercises	313
9	Non-stationarity	315
9.1	Introduction	315
9.2	Deterministic Trend	317
9.3	Integrated Series	320
9.4	Contrasting Stationary and Integrated Series	324
9.5	Spurious Regression	328
9.6	The Dickey–Fuller Distribution	331
9.7	Testing the Null Hypothesis of a Unit-Root	333
9.8	Exercises	336
10	Cointegration	339
10.1	Introduction	339
10.2	Engle and Granger Representation Theorem	340
10.3	Estimating a Single Cointegrating Vector	349
10.4	Testing Rank Zero Against Rank Equal to One	353
10.5	Multiple Equation Cointegration	358
10.6	Exercises	374
11	Automatic Variable Selection	379
11.1	Introduction	379
11.2	Terminology and Basic Gets Concepts	383
11.3	The Search Tree	386
11.4	Overall Test Size and the Retention Rate of Irrelevant Variables	391
11.5	Retaining Relevant Variables	396
11.6	The Roles of $I(1)$ -variables and of Misspecification Testing	397
11.7	Automatic Detection of Structural Breaks	400

11.8	Gets When the GUM is Under-specified, and Keeping Theory Variables	401
11.9	Exercises	402
12	Model-Based Forecasting	405
12.1	Introduction	405
12.2	Basic Concepts and Results from Forecasting Theory . .	408
12.3	Reference Properties of VAR-Based Forecasts	411
12.4	An Illustration of the Reference Case	419
12.5	Forecasting in a Non-stationary World	422
12.6	Forecast Failures in Practice	428
12.7	Add-Factors and Intercept Corrections	430
12.8	Combination of Forecasts	433
12.9	Naive Forecasts	436
12.10	Some Pros and Cons of Model-Based Forecasting	438
12.11	Exercises	442
A	A Growth Model and RBC Theory	445
A.1	The Solow Model in Discrete Time	445
A.2	Real Business Cycle Model	449
B	Spectral Analysis	457
B.1	Introduction	457
B.2	Frequency and Period	458
B.3	Discrete Fourier Transformation and the Periodogram .	459
B.4	Infinite Fourier Transformation	461
B.5	Power Spectral Density Function	462
B.6	PSD of ARMA Series	463
B.7	Linear Filters, Power-Shift and Phase-Shift	468
B.8	Regression in the Spectral Domain: The Cross-Spectrum and Coherency	470
B.9	The Power Spectrum of ARIMA Series: The Typical Spectral Shape	473
B.10	Seasonal Integration	474
B.11	Estimation	477

C	Answer Notes to Exercises	479
C.1	Chapter 1 Answers	479
C.2	Chapter 2 Answers	482
C.3	Chapter 3 Answers	495
C.4	Chapter 4 Answers	500
C.5	Chapter 5 Answers	504
C.6	Chapter 6 Answers	511
C.7	Chapter 7 Answers	519
C.8	Chapter 8 Answers	525
C.9	Chapter 9 Answers	526
C.10	Chapter 10 Answers	529
C.11	Chapter 11 Answers	535
C.12	Chapter 12 Answers	539
	<i>Bibliography</i>	545
	<i>Index</i>	557