

University of Pittsburgh
International Finance
Problem Set 3

1 Data crunching (25 points)

Replicate Table 1 for Arellano (2008) for Greece. For the default episode, use Q1.2012. For the business cycle statistics, use Q1.1980-Q3.2014.

2 Computation (25 points)

Solve the model in Arellano (2008) using a package of your choice. Set the parameters to the benchmark in the paper (or change them if you like) and produce business cycle statistics comparable to table 4 in Arellano (2008). Write 1 page highlighting success and failures of the model and explain why it is so. Feed in the sequence of output shocks for Argentina Q2.1993 to 2001Q2 to produce figure 5 in Arellano (2008)

3 More computation (25 points)

Now estimate the endowment process using the output series of Greece. Are they different from Argentina? Using the estimated process for Greece (for all other parameters use the baseline values), solve the model and report the business cycle statistics as in table 4 in Arellano (2008). Feed in the output shocks for Greece Q1.2005 to Q2.2012 to generate the equivalent of figure 5.

4 Even more computation (25 points)

Now change the output cost to a proportional output cost, i.e. $y^d = (1 - \gamma)y$. Set $\gamma = 0.05$. How do the results change?