

The Loud Silence of the Pretzel Bloggers*

Fabio Ghironi

University of Washington, CEPR, and NBER

Director, Research Program in International Trade and Macroeconomics, Central Bank Research Association

April 7, 2017

I recently had two conversations with Bloomberg View columnist and blogger Noah Smith that convinced me of something: Bloggers will twist themselves into pretzels rather than acknowledging that mainstream macroeconomics (often referred to as DSGE macro) delivered a number of valuable insights over the years—before and after the global crisis of 2007-08 and the Great Recession.

The first conversation took place on March 28, 2017, after Noah tweeted that “top mainstream macroeconomist Larry Christiano” was admitting that “Paul Krugman was right and everyone else was wrong” in a paper that Larry published in the Minneapolis Fed *Economic Policy Papers* series.¹ My reply to that tweet began the conversation that follows.



Fabio Ghironi @FabioGhironi · Mar 28

Replying to @Noahpinion

.@Noahpinion I don't think this is what Larry is saying. @paulkrugman was right, but he was not alone in thinking govt has a role to play. >

Neglected paradigms

At its heart, the narrative described above characterizes the Great Recession as the response of the economy to a negative shock to the demand for goods all across the board. This is very much in the spirit of the traditional macroeconomic paradigm captured by the famous IS-LM (or Hicks-Hansen) model,⁹ which places demand shocks like this at the heart of its theory of business cycle fluctuations. Similarly, the paradox-of-thrift argument¹⁰ is also expressed naturally in the IS-LM model.

The IS-LM paradigm, together with the paradox of thrift and the notion that a decision by a group of people¹¹ could give rise to a welfare-reducing drop in output, had been largely discredited among professional macroeconomists since the 1980s. But the Great Recession seems impossible to understand without invoking paradox-of-thrift logic and appealing to shocks in aggregate demand. As a consequence, the modern equivalent of the IS-LM model—the New Keynesian model—has returned to center stage.¹² (To be fair, the return of the IS-LM model began in the late 1990s, but the Great Recession dramatically accelerated the process.)

The return of the dynamic version of the IS-LM model is revolutionary because that model is closely allied with the view that the economic system can sometimes become dysfunctional, necessitating some form of government intervention. This is a big shift from the dominant view in the macroeconomics profession in the wake of the costly high inflation of the 1970s. Because that inflation was viewed as a failure of policy, many economists in the 1980s were comfortable with models that imply markets work well by themselves and government intervention is typically unproductive.

* The views in this document are entirely personal and do not reflect the views or policies of the CEPR, NBER, and the Central Bank Research Association.

¹ Christiano (2017): “[The Great Recession: A Macroeconomic Earthquake](#),” *Economic Policy Paper* 17-01, Federal Reserve Bank of Minneapolis.



Noah Smith @Noahpinion · Mar 28

I think this is pretty close to exactly what Krugman was saying.



Fabio Ghironi @FabioGhironi · Mar 28

But how would that imply your interpretation of what Larry wrote is correct? I don't think Larry said "everyone else was wrong."



Noah Smith @Noahpinion · Mar 28

Oh, just because no one was using ZLB-NK or anything equivalent before the crisis.



Fabio Ghironi @FabioGhironi · Mar 28

That's wrong. Plenty of ppl were working on ZLB-NK stuff long before the crisis. Japan took care of triggering interest in that.



Noah Smith @Noahpinion · Mar 28

I guess, I never once saw it in the pre-2007 literature. And no one ever ever talked about it, even New Keynesian enthusiasts.



Fabio Ghironi @FabioGhironi · Mar 28

A ton of papers were written & published b/w late 90s & early 00s. Many references here: nber.org/papers/w10195 >



Fabio Ghironi @FabioGhironi · Mar 28

See also work by Schmitt-Grohe & Uribe. NK enthusiasts were very enthusiastic about the topic!



Noah Smith @Noahpinion · Mar 28

So Christiano is wrong in his characterization of the field before the crisis? 🤔



Fabio Ghironi @FabioGhironi · Mar 28

I think Christiano should have mentioned that a lot of NK-ZLB work was done before the crisis because of Japan. >





Fabio Ghironi @FabioGhironi · Mar 28

A chunk of that work happened in the open economy NK lit, which is why closed econ ppl may have missed it. But much also in >

1 1



Fabio Ghironi @FabioGhironi · Mar 28

closed-economy lit. The names involved are pretty std players in the NK crowd, so hard to miss completely. Plus, b/c of nature >

1 1



Fabio Ghironi @FabioGhironi · Mar 28

of Japan slump, some ppl started to think about financial mkt stuff in NK macro before 07-08, even in regard to other countries>

1 1



Fabio Ghironi @FabioGhironi · Mar 28

Here's an example: [sciencedirect.com/science/articl...](https://www.sciencedirect.com/science/article/pii/S0165176509000000) (published in 2010, but written long before, no ZLB, but not on Japan). >

1 1 2



Fabio Ghironi @FabioGhironi · Mar 28

In sum, statement that NK ppl other than Krugman started thinking on ZLB &/or financial mkt seriously only w crisis is wrong. >

2 2



Noah Smith @Noahpinion · Mar 28

Fair enough. I just never heard of it or saw it (ZLB stuff). I do know that ppl considered financial mkts for a long time.

1



Tony Yates @t0nyyates · Mar 28

see JMCB conference volume of 2000

1 1 4



Fabio Ghironi @FabioGhironi · Mar 28

Yep. That's a great example. And it is easy to find many more.



Fabio Ghironi @FabioGhironi · Mar 28

Fact 1: NK crowd was into ZLB (& financial mkts) long before 07.

Fact 2: A lot of this work was done in DSGE models.>



Noah Smith @Noahpinion · Mar 28

OK, guys, I'm going to look into this. But if I find out you guys are feeding me a line... ;-)



Noah Smith @Noahpinion · Mar 28

Anyway, I'd like to know whether you agree with the Christiano assessment in the quote I posted.



Fabio Ghironi @FabioGhironi · Mar 28

I agree that crisis & Great Recession sd have settled once & for all the dispute on importance of demand-side forces>



Fabio Ghironi @FabioGhironi · Mar 28

& on the scope for govt/central bank role in improving outcomes. In that sense, I agree w crisis & GR accelerating >



Fabio Ghironi @FabioGhironi · Mar 28

broader acceptance of dynamic IS-LM as relevant benchmark. I just see the crisis & GR as a bit less of a watershed >





Noah Smith @Noahpinion · Mar 28

I kind of think the same. I'm a little surprised Christiano says it was such a watershed.



1



1



Fabio Ghironi @FabioGhironi · Mar 28

Yep. Me too b/c Larry should remember all this work that Tony and I pointed to (at least the closed econ stuff). >



1



Fabio Ghironi

@FabioGhironi

Replying to @FabioGhironi @Noahpinion @t0nyyates

I look forward to continuing the conversation once you've done a bit more digging. Have fun!

11:19 PM - 28 Mar 2017

After this tweet, I returned to something I meant to say about the crisis and Great Recession as watershed for macro:



After this exchange, Noah corrected the text of his original tweet (of which I did not take a screenshot) as follows:



Noah Smith @Noahpinion · Mar 28

Top mainstream macroeconomist Larry Christiano: The Great Recession made us remember the importance of IS-LM: minneapolisfed.org/~media/files/ ...

Neglected paradigms

At its heart, the narrative described above characterizes the Great Recession as the response of the economy to a negative shock to the demand for goods all across the board. This is very much in the spirit of the traditional macroeconomic paradigm captured by the famous IS-LM (or Hicks-Hansen) model,⁹ which places demand shocks like this at the heart of its theory of business cycle fluctuations. Similarly, the paradox-of-thrift argument¹⁰ is also expressed naturally in the IS-LM model.

The IS-LM paradigm, together with the paradox of thrift and the notion that a decision by a group of people¹¹ could give rise to a welfare-reducing drop in output, had been largely discredited among professional macroeconomists since the 1980s. But the Great Recession seems impossible to understand without invoking paradox-of-thrift logic and appealing to shocks in aggregate demand. As a consequence, the modern equivalent of the IS-LM model—the New Keynesian model—has returned to center stage.¹² (To be fair, the return of the IS-LM model began in the late 1990s, but the Great Recession dramatically accelerated the process.)

The return of the dynamic version of the IS-LM model is revolutionary because that model is closely allied with the view that the economic system can sometimes become dysfunctional, necessitating some form of government intervention. This is a big shift from the dominant view in the macroeconomics profession in the wake of the costly high inflation of the 1970s. Because that inflation was viewed as a failure of policy, many economists in the 1980s were comfortable with models that imply markets work well by themselves and government intervention is typically unproductive.

5 42 78

I cannot prove it with the screenshot of the original tweet, but if you choose to believe me, I guess Tony Yates and I succeeded in convincing Noah that Krugman was not alone in “being right.” I thought we might even have convinced him that DSGE macro had delivered some important insights after all.

My next conversation with Noah happened on April 5, 2017. It was triggered by Noah’s Bloomberg View column “[When Economics Failed](#)” (April 4, 2017), and it began with my tweet below:



Fabio Ghironi

@FabioGhironi



Must have been a boring day at @BV as @Noahpinion is rehashing a stale, bad argument against DSGE macro:



When Economics Failed

The tools the profession uses to forecast recessions still are a long way from being up to the task.

bloomberg.com

This prompted the following exchange:



Noah Smith @Noahpinion · Apr 5

Replying to @FabioGhironi

Do you have any response to the third paragraph??



1



Fabio Ghironi @FabioGhironi · Apr 5

It wouldn't convince you anyway. You decided long ago that DSGE macro is wrong & useless, & I don't think anything I cd say wd change that.



1



3



Noah Smith @Noahpinion · Apr 5

I don't think it's wrong and useless, but I think weak forecasting performance is a bad sign for models that currently exist.



2



Markku Stenborg @markkuilmari · Apr 5

Someone actually does forecasting w/ DSGE alone?



1



Noah Smith @Noahpinion · Apr 5

Some folks claim you now can, but it doesn't look great.



1



Markku Stenborg @markkuilmari · Apr 5

Definitely a wrong way to use DSGE. Useful but not the only g



2



Noah Smith @Noahpinion · Apr 5

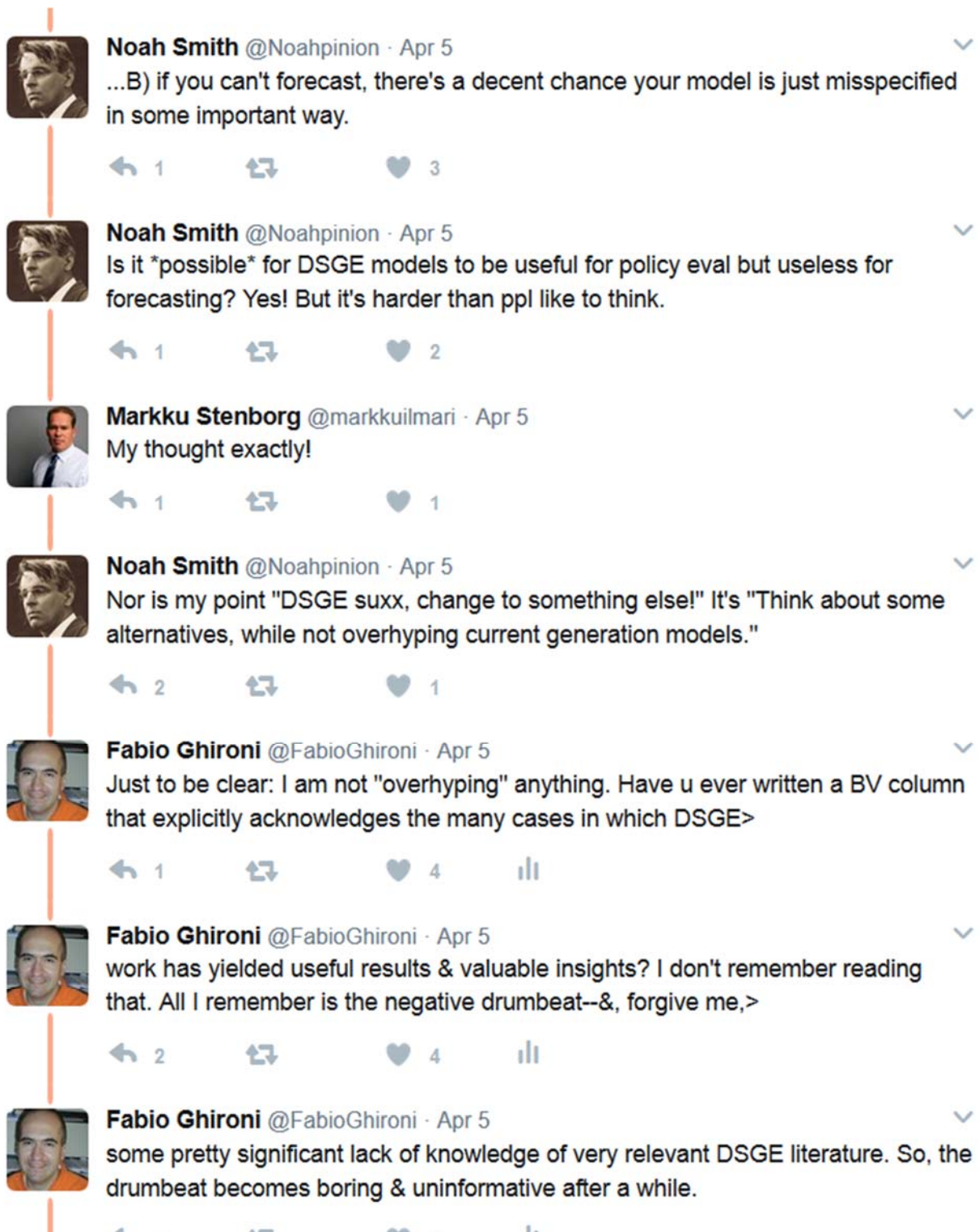
My points are A) if you can't forecast, there's so much noise that it's hard to tell which model to use for policy eval, and...



1



2



As I was typing my responses, Noah was also typing:



Fabio Ghironi @FabioGhironi · Apr 5

Just to be clear: I am not "overhyping" anything. Have u ever written a BV column that explicitly acknowledges the many cases in which DSGE>

1 4



Fabio Ghironi @FabioGhironi · Apr 5

work has yielded useful results & valuable insights? I don't remember reading that. All I remember is the negative drumbeat--&, forgive me,>

2 4



Noah Smith @Noahpinion · Apr 5

Oh, because when I talk positively about models, it's about specific ones:



A Wealth Tax Looks Like It Can Make a Country Richer

The trade-off would be exempting profits and capital gains, encouraging people to put money to more productive use.

[bloomberg.com](https://www.bloomberg.com)

2



Fabio Ghironi @FabioGhironi · Apr 5

& is it by chance that u omit that Fatih et al's model includes a lot of features you've been criticizing all over:

fguvenendotcom.files.wordpress.com/2014/04/gkkoc_...

1



Noah Smith @Noahpinion · Apr 5

It certainly does. I view current DSGE models as capable of communicating interesting ideas, but not quantitatively describing the economy.

2



Noah Smith @Noahpinion · Apr 5

In this respect, they're like models written in words. The math is sometimes a useful explanatory tool (though often the opposite)...

2



Noah Smith @Noahpinion · Apr 5

But the quest to do better - to have models that reliably predict the quantitative effects of policy - remains unfulfilled, I think.

1



Fabio Ghironi @FabioGhironi · Apr 5

Like you, I believe there is much to do to improve our models. I think the quest to do better will never end, & that's part of the "fun." >

2



Noah Smith @Noahpinion · Apr 5

I don't want to rain on anyone's fun!!

But I do kind of want to prod people to at least *try* improvement via radical change... :-)

1



Noah Smith @Noahpinion · Apr 5

I certainly am not trying to tell you or other DSGE researchers that your careers are worthless or bad...don't take it personally!



2



Fabio Ghironi @FabioGhironi · Apr 5

I'm certainly not taking this personally--except I'll say I don't think of myself as a DSGE researcher. I just think, of all bloggers, >



1



Fabio Ghironi @FabioGhironi · Apr 5

you're in a better position than others to give a more balanced view of how macro has been evolving than what transpires from your writing.



1



2



Noah Smith @Noahpinion · Apr 5

Well, I do praise macro for A) adding finance to models, and B) becoming more empirical.



1



2



Fabio Ghironi @FabioGhironi · Apr 5

My suggestion for item (C): when you praise a model for delivering interesting results, do mention that it incorporates all that bad stuff.

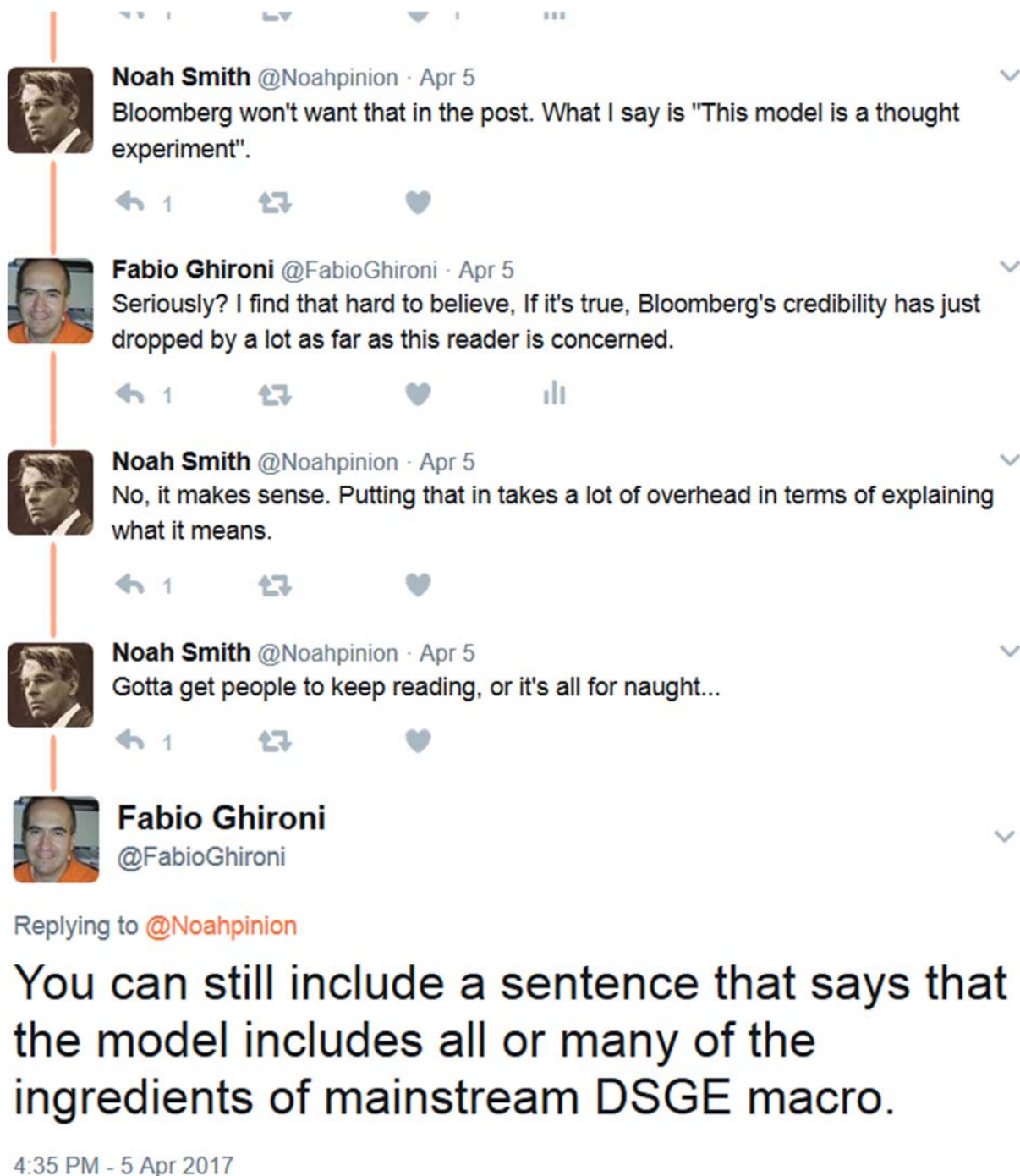


1



1





This was the end of the conversation.

My conclusions from the two conversations: (1) A columnist and blogger with a Ph.D. in economics from a highly rated department (and with almost 57k Twitter followers) displays significant lack of knowledge of the mainstream macro he often criticizes. (2) Even when this blogger discusses and praises interesting results and insights from macro papers that incorporate many (if not all) of the assumptions for which he criticizes mainstream macro, the blogger carefully avoids acknowledging that this is the case, claiming that it is his publisher that makes it impossible for him to include even simple versions of that acknowledgment.

You can draw your own conclusions from all this. From my perspective, until I am proven wrong by his writing, the key thing I learned is that Noah (and—I am willing to bet—the vast majority of other bloggers and columnists who share his views) will twist himself into a pretzel rather than admitting (even implicitly) that the macro he so likes to criticize has produced and continues to produce a number of valuable results and insights.

I greatly enjoy reading Noah's columns and I agree with him on many issues, but—in my opinion—his loud silence on the merits of mainstream macro modeling greatly reduces his credibility when he comments on macro methodology. And I wonder if he will re-tweet my tweet on this note to his 57k followers...

PS: Just to make it clear, as I tweeted in my second conversation with Noah, I do not think of myself as a DSGE researcher. I think of myself as an applied macro theorist, with interests mainly in international macroeconomics. I find questions of positive or normative nature that I am interested in, often motivated by ongoing events and policy debates, and I develop models to address the questions. Over the course of my career, I have learned much from and written plenty of non-DSGE models. I have been working mostly with DSGE models for the last 15 years or so because I think they are appropriate for the questions I have been working on. This does not mean that I am married to DSGE (or any other modeling technique). But I like fairness in the evaluation of any methodology and in the information that is provided to the public. If you are curious about my work, you can find it [here](#).