



## Uncertainty within Economic Models (World Scientific Series in Economic Theory) (Volume 6)

By Lars Peter Hansen

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Written by Lars Peter Hansen (Nobel Laureate in Economics, 2013) and Thomas Sargent (Nobel Laureate in Economics, 2011), *Uncertainty within Economic Models* includes articles adapting and applying robust control theory to problems in economics and finance. This book extends rational expectations models by including agents who doubt their models and adopt precautionary decisions designed to protect themselves from adverse consequences of model misspecification. This behavior has consequences for what are ordinarily interpreted as market prices of risk, but big parts of which should actually be interpreted as market prices of model uncertainty. The chapters discuss ways of calibrating agents' fears of model misspecification in quantitative contexts.

Readership: Graduate students; researchers and economists interested in Econometrics; Macroeconomics and Dynamic Programming.

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## **Editorial Review**

### **Review**

*"Studying this work in real time taught me a lot, but seeing it laid out in conceptual, rather than chronological, order provides even clearer insights into the evolution of this provocative line of research. Hansen and Sargent are two of the best economists of our time, they are also among the most dedicated teachers in our profession. They have once again moved the research frontier, and with this book provide a roadmap for the rest of us to follow. This is a must-have for anyone interested in modeling uncertainty, ambiguity and robustness." -- Stanley E Zin, William R Berkley Professor of Economics and Business, Leonard N Stern School of Business New York University*

### **From the Inside Flap**

Uncertainty within Economic Models is a collection of papers adapting and applying robust control theory to problems in economics and finance. This book extends rational expectations models by including agents who doubt their models and adopt precautionary decisions designed to protect themselves from adverse consequences of model misspecification. This behavior has consequences for what are ordinarily interpreted as market prices of risk, but big parts of which should actually be interpreted as market prices of model uncertainty. The chapters discuss ways of calibrating agents' fears of model misspecification in quantitative contexts.

### **About the Author**

**Lars Peter Hansen**, the David Rockefeller Distinguished Service Professor at the University of Chicago, is an internationally known leader in economic dynamics. He was awarded the 2013 Nobel Prize in Economics, shared with Eugene F Fama (University of Chicago) and Robert J Shiller (Yale University), for their empirical analysis of asset prices." Hansen guides the scholarly direction of the Becker Friedman Institute and chairs the Institute Research Council. He was one of the forces behind the 2008 creation of the Milton Friedman Institute, the predecessor of the Becker Friedman Institute, and served as its founding director.

Hansen's work explores formal implications of dynamic economic models in which decision makers face uncertain environments. The main theme of his research has been to devise and apply econometric methods that are consistent with the probabilistic framework of the economic models under investigation. His work has implications for consumption, savings investment, and asset pricing.

Hansen's early research in econometrics was aimed at developing time series statistical methods to investigate one part of an economic model without having to fully specify and estimate all of the model ingredients. The applications he explored with several coauthors included systems that are rich enough to support models of asset valuation and to identify and clarify empirical puzzles, where real-world financial and economic data were at odds with prevailing academic models.

He continues to explore, analyze, and interpret implications of dynamic economic models in environments with uncertainty from a time-series perspective. His recent research explores ways to quantify intertemporal risk-return tradeoffs and ways to model economic behavior when decision makers are uncertain about how to forecast future economic events.

Hansen won the 2010 BBVA Foundation Frontiers of Knowledge Award in the Economics, Finance and Management "for making fundamental contributions to our understanding of how economic actors cope with

risky and changing environments." He also received the CME Group-MSRI Prize in Innovative Quantitative Applications in 2008 and the Erwin Plein Nemmers Prize in Economics from Northwestern University in 2006.

He was selected to deliver the Princeton Lectures in Finance at the Bendheim Center for Finance in December 2010, the Tjalling C Koopmans Memorial Lectures at Yale in September 2008, and the Third Toulouse Lectures in Economics at the Université de Toulouse in May 2005.

**Thomas J Sargent** is Professor of Economics at New York University. He was awarded the 2011 Nobel Prize in Economics, shared with Princeton University's Christopher Sims, for their empirical research on cause and effect in the macroeconomy. He received his bachelors degree from the University of California at Berkeley, winning the medal as the university most distinguished scholar in the Class of 1964, and obtained his PhD at Harvard University in 1968. He has been Professor of Economics at the University of Minnesota, the David Rockefeller Professor at the University of Chicago, and the Donald Lucas Professor of Economics at Stanford University. He has been a Senior Fellow at the Hoover Institution since 1987. He is a Fellow of the National Academy of Sciences, the American Academy of Arts and Sciences, and the Econometric Society. He has been President of the American Economic Association, the Econometric Society, and the Society for Economic Dynamics. In his Nobel speech in Stockholm he described himself as someone who aspires to use statistics and economic theory to understand how governments and markets can improve peoples' lives.

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