Harvard University, fall 2017, Syllabus for:
Economics 2148 - Topics in Econometrics

Part I: Advances in causality and foundations of machine learning

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Overview and Objectives

Economics 2148, one of the second-year econometrics field classes, will be co-taught by Elie Tamer and me. This is is the Syllabus for the first half of the course.

We will begin the class with a survey of the literature on identification using instrumental variables, taking the linear model as a point of departure. The linear model imposes strong restrictions on the heterogeneity of causal effects. Generalizing this model to allow for nonlinear and heterogeneous effects leads to a variety of approaches discussed in the literature, including a re-interpretation of classic estimands as LATE, bounds on objects such as the ATE that are not point identified, conditional moment restrictions, and control function approaches.

The next part of class will cover some of the theoretical foundations of machine learning, including regularization and data-driven choice of tuning parameters. We will discuss in some detail the canonical normal
means model. In this model, we will motivate shrinkage estimators in different ways, and will prove the famous result that shrinkage estimators can uniformly dominate conventional estimators. We will then move from normal means to function estimation using Gaussian process priors. We will show the equivalence of (empirical) Bayes estimation using such priors to penalized least squares regression with penalties corresponding to so-called reproducing kernel Hilbert space norms. The first half of 2148 concludes with some applications of Gaussian process priors to experimental design and to optimal taxation.

For both instrumental variables and shrinkage will briefly review some of the foundations that were covered in Economics 2110 last year.

Requirements and policies

Your grade for Economics 2148 will be determined by both the first and second half of the class with equal weights. For the first half of the class, you are asked to complete two computer-based problem sets, and to submit summaries of two papers of your choice from the references at the end of this Syllabus. I am happy to make recommendations if you are not sure which ones to pick. Please upload both your problem set solutions and your summaries via Canvas. These assignments contribute to your grade as follows.

1. Two summaries of about 3 pages length each (7% of grade each).

2. Two problem set solutions (7% of grade each).

3. In-class midterm exam on October 12 (22% of grade).

Additionally, the slides contain a lot of “practice problems,” which you will have to solve in class. The idea is to have you complete most of the proofs, after I pointed you in the right direction. After a few minutes, we will discuss the solutions to these problems. These problems provide good guidance for what you might expect from the midterm exam.

To help me improve the course, I will ask you to give me anonymous feedback at some point, writing what you like about the class and what you think I should change.

I encourage you to come to office hours with any questions. If you need any special accommodations for physical or medical reasons, please see me after class or send me an email.
Outline of the course

Instrumental variables part I – origins and binary treatment

- Origins of instrumental variables: Systems of linear structural equations
- Strong restriction: Constant causal effects.
- Modern perspective: Potential outcomes, allow for heterogeneity of causal effects
- Keep IV estimand, reinterpret it in more general setting: Local Average Treatment Effect (LATE)
- Keep object of interest: Average Treatment Effect (ATE) Partial identification (Bounds)

Instrumental variables part II – continuous treatment

- Restricting heterogeneity in the structural equation: Nonparametric IV (conditional moment equalities)
- Restricting heterogeneity in the first stage: Control functions
- Linear IV: Continuous version of LATE

Review of decision theory

- Basic definitions
- Optimality criteria
- Relationships between optimality criteria
- Analogies to microeconomics
- Two justifications of the Bayesian approach
Shrinkage in the normal means model

- Setup: the normal means model $X \sim N(\theta, I_k)$ and the canonical estimation problem with loss $\|\hat{\theta} - \theta\|^2$.

- The James-Stein (JS) shrinkage estimator.

- Three ways to arrive at the JS estimator (almost):
  1. Reverse regression of $\theta_i$ on $X_i$.
  2. Empirical Bayes: random effects model for $\theta_i$.
  3. Shrinkage factor minimizing Stein’s Unbiased Risk Estimate.

- Proof that JS uniformly dominates $X$ as estimator of $\theta$.

- The normal means model as asymptotic approximation.

Gaussian process priors, reproducing kernel Hilbert spaces, and Splines

- 6 equivalent representations of the posterior mean in the normal-normal model.

- Gaussian process priors for regression functions.

- Reproducing Kernel Hilbert Spaces and splines.

Applications of Gaussian process priors from my own work

- Optimal treatment assignment in experiments.
  - Setting: Treatment assignment given baseline covariates
  - General decision theory result:
    Non-random rules dominate random rules
  - Prior for expectation of potential outcomes given covariates
  - Expression for MSE of estimator for ATE to minimize by treatment assignment

- Optimal insurance and taxation.
  - Review: Envelope theorem.
  - Economic setting: Co-insurance rate for health insurance
  - Statistical setting: prior for behavioral average response function
  - Expression for posterior expected social welfare to maximize by choice of co-insurance rate
References

Instrumental variables – binary treatment


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