

Fall 2019

ECONOMICS 1410 / KENNEDY SCHOOL SUP-125
Public Economics: Designing Government Policy
Professors Stefanie Stantcheva and Stan Veuger

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Course Description: This course analyzes what role the government plays and should play in a market economy, especially those policies that work through taxes and government spending. It covers topics such as tax and welfare policy, unemployment insurance, environmental protection, social security, and state and local policy. The course emphasizes recent empirical research on policy issues and will teach students how to conduct such studies.

The first half of the course, taught mainly by Professor Stantcheva, will cover the basic principles of public economics. These principles will be used to shed light on current questions and debates on tax policy. The second half of the course, taught mainly by Professor Veuger, will discuss recent research on taxation, health care, the regulatory state, political economy, and state and local policy. This part of the course will also teach students current econometric methods used in public economics.

Prerequisites: Economics 1010a or 1011a or permission of the instructors. Familiarity with multivariate calculus and econometrics (at the level of economics 1123 or 1126) is desirable.

Course Mechanics:

- 1) Lectures – Two lectures per week. MW 3:00 to 4:15 in Sever Hall 308.
- 2) Sections – One per week. Room and time **TBA**.
- 3) Readings – Jonathan Gruber, *Public Finance and Public Policy (5th edition)*, is the optional but recommended textbook. Other readings are listed below.
- 4) Assignments will be posted on the course website, which should be checked regularly: <https://canvas.harvard.edu/courses/60932>

Grading: Grades will be based on a midterm exam (30 percent), final exam (50 percent), and problem sets (20 percent). Because you will have two weeks to complete each problem set and in order to allow the solutions to be posted quickly on the course webpage, late problem sets will not be accepted.

Term Paper Option: Students may write a term paper that contains *original* research on a topic in public economics. The term paper satisfies the Economics Department's writing requirement for economics concentrators. See below for more details on this option.

Academic Accommodations: Students needing academic accommodations because of a documented disability must present their Faculty Letter from the Accessible Education Office (AEO) by Monday, September 23.

Collaboration: Discussion and the exchange of ideas are essential to academic work. You are encouraged to consult with your classmates on the choice of paper topics and to share sources. You may find it useful to discuss your chosen topic with your peers, particularly if you are working on the same topic as a classmate. However, you should ensure that any written work you submit for evaluation is the result of your own research and writing and that it reflects your own approach to the topic. You must also adhere to standard citation practices in this discipline and properly cite any

books, articles, websites, lectures, etc. that have helped you with your work. If you received any help with your writing (e.g., feedback on drafts), you must also acknowledge this assistance.

No collaboration of any kind is allowed during exams. On problem sets, you may consult with your classmates and the teaching staff. However, you must write up your own solutions in your own words based on your own understanding.

Frequently asked questions:

1. Textbook. You are welcome to buy any edition of the textbook. The textbook provides useful background material but the lectures do not follow any book. Therefore, attending class is critical. The textbook would be an especially useful resource for students interested in writing a senior honors thesis or term paper on a policy related topic.
2. Grading option. The course must be taken for a letter grade. However, you are welcome to sit in on the lectures if you choose not to take the class for credit.
3. Adding the course late. The last day to add the course without a fee is September 24. You may add the course until this date, but only if you have attended the lectures and kept up with the readings. Borrowing notes from others is not sufficient. Therefore, if you think that you may want to take the course for credit, you should attend class and complete the coursework on-time (e.g., readings, problem sets, term paper proposals), as if you are enrolled in the course. We may ask to see your class notes before signing your add form.
4. Cross-registration and website access. The course is open to students from other faculties and from MIT. In order to view the files on the course website, students enrolled in the course will need to log-in with a Harvard University ID and pin. Students enrolled through the Kennedy School course or who otherwise do not have a HUID can sign up for an XID at:

<https://xid.harvard.edu/xid-apps/displaySSCreateForm.do>
5. Course meetings. The course meets on Monday and Wednesday. A detailed lecture schedule is outlined below.
6. Attendance. Students who are enrolled in the course for credit are responsible for all material covered and any course announcements made in lecture and section. You should only enroll in the class for credit if you can attend class regularly. Students who have had to miss more than one or two lectures in the past have had difficulty on problem sets and exams and have not done well in the course.
7. Other readings. Academic journal articles listed on the reading list below will be distributed electronically for your convenience. Please see the course website for details on the procedure that we will use. All articles should also be available to Harvard College students for free by searching for the title in Google Scholar:

<http://scholar.google.com.ezp-prod1.hul.harvard.edu/schhp?inst=harvard.edu>

or as working papers through the National Bureau of Economic Research website:

<http://www.nber.org.ezp-prod1.hul.harvard.edu/>

8. Exams. The midterm exam will be held in class on October 23. You should only enroll in the class for credit if you can be in attendance to take the midterm on this date. The date, time, and location of the final exam will be assigned by the registrar's office.

No notes or books are allowed during either exam. You may use a calculator.

Term paper option

Students writing a term paper will not have to complete the assignments. Instead, the term paper will count for 20 percent of the grade. A term paper proposal is due on 9/24. The completed term paper is due 3 days before the final exam.

Most term papers use Stata, which is available for download at: <https://downloads.fas.harvard.edu/>

Papers from previous years include the following.

1. The effect of the Bush tax cuts on the spread between tax-exempt and taxable securities (using data on yields from Baker Library at HBS)
2. Using asset prices to measure the general equilibrium incidence of Supreme Court rulings on producers of GMO foods (using Fama-French and CRSP data from the WRDS database)
3. The effect of professional sports franchises and stadiums on employment and local economic growth
4. The effect of top marginal tax rates on executive compensation (using ExecuComp data from the WRDS database)
5. Gender inequality and intergenerational mobility (using female-male wage gaps constructed from the CPS and intergenerational mobility data from the Equality of Opportunity Project)

LECTURE DATES

1. Wednesday, September 4 Veuger - Intro; Empirical Methods for Public Economics
2. Monday, September 9 Stantcheva - Income Distribution, Poverty, Taxes and Transfers
3. Wednesday, September 11 Stantcheva - Theoretical Tools for Public Economics
4. Monday, September 16 Stantcheva - Tax Incidence
5. Wednesday, September 18 Stantcheva - Optimal Labor Income Taxation
6. Monday, September 23 Stantcheva - Taxes and Labor Supply [**AEO letters due; PS1 assigned**]
7. Wednesday, September 25 Stantcheva - Taxes and Reported Income
- Monday, September 30*
8. Wednesday, October 2 *No Class (Rosh Hashanah)*
Stantcheva - Externalities
9. Monday, October 7 Stantcheva - Public Goods
- Wednesday, October 9* *No Class (Yom Kippur)*
10. Friday, October 11 Stantcheva - Social Insurance (intro) and Health Insurance (Part I) [**PS1 due**]
- Monday, October 14* *No Class (Columbus Day)*
11. Wednesday, October 16 Veuger - The Federal Budget
12. Monday, October 21 Stantcheva - Stantcheva: Health Insurance (Part II)
13. Wednesday, October 23 **Midterm**
14. Friday, October 25 Veuger – Social Security
15. Monday, October 28 Veuger – Tax Reform
16. Wednesday, October 30 Veuger – Business Taxation
17. Monday, November 4 Veuger – Politics and Policy
18. Wednesday, November 6 Veuger – Politics and Policy / Regulation [**PS 2 assigned**]
- Monday, November 11* *No Class (Veterans Day)*
19. Wednesday, November 13 Veuger - Regulation
20. Monday, November 18 Veuger – Multilevel Government
21. Wednesday, November 20 Veuger – Multilevel Government
22. Monday, November 25 Veuger – Health Care Reform [**PS 2 due**]
- Wednesday, November 27* *No Class (Thanksgiving)*
23. Monday, December 2 Stantcheva - Unemployment Insurance, Disability Insurance, Workers' Compensation; Review

READINGS

September 4: Introduction and Empirical Methods for Public Economics

Veuger

Gruber, Chapter 3

J. Angrist and J.-S. Pischke (2010) “The Credibility Revolution in Empirical Economics: How Better Research Design is Taking the Con out of Econometrics”, *Journal of Economic Perspectives* 24(2): 3-30.

H. Low and C. Meghir (2017) “The Use of Structural Models in Econometrics,” *Journal of Economic Perspectives* 31(2): 33-58. (optional)

W.G. Gale (2019) “Government at a Glance.” In: *Fiscal Therapy: Curing America’s Debt Addiction and Investing in the Future*. New York, NY: Oxford University Press. 17-32.

L. Linden and J. Rockoff (2008) “There Goes the Neighborhood? Estimates of the Impact of Crime Risk on Property Values from Megan’s Laws,” *American Economic Review* 98(3): 1103-1127. (optional)

H. Allcott, R. Diamond, and J.-P. Dubé (2018) “The Geography of Poverty and Nutrition: Food Deserts and Food Choices Across the United States,” *NBER Working Paper* 24094. (optional)

R. Diamond and T.J. McQuade (2019) “Who Wants Affordable Housing in their Backyard? An Equilibrium Analysis of Low Income Property Development,” *Journal of Political Economy*, 127(3): 1063-1117. (optional)

September 9: Income Distribution, Poverty, Taxes and Transfers

Stantcheva

Gruber, Chapters 17 and 18

Piketty, Thomas, and Emmanuel Saez (2003) “Income Inequality in the United States, 1913-1998,” *The Quarterly Journal of Economics* 118(1): 1-41. (optional)

Atkinson, Anthony B., Thomas Piketty, and Emmanuel Saez (2011) “Top Incomes in the Long-Run of History,” *Journal of Economic Literature* 49(1): 3-71. (optional)

September 11: Theoretical Tools for Public Economics

Stantcheva

Gruber, Chapter 2

Saez, Emmanuel and Stefanie Stantcheva (2016) “Generalized Social Marginal Welfare Weights for Optimal Tax Theory,” *American Economic Review* 106(1): 24-45.

September 16: Tax Incidence

Stantcheva

Gruber, Chapter 19

Chetty, Raj, Adam Looney, and Kory Kroft (2009) "Salience and Taxation: Theory and Evidence," *American Economic Review* 99(4): 1145-1177. (optional)

Doyle Jr, Joseph J., and Krislert Samphantharak (2008) "\$2.00 Gas! Studying the Effects of a Gas Tax Moratorium," *Journal of Public Economics* 92(3): 869-884. (optional)

September 18: Optimal Labor Income Taxation

Stantcheva

Gruber, Chapter 20 and 21

Diamond, Peter, and Emmanuel Saez (2011) "From Basic Research to Policy Recommendations: The Case for a Progressive Tax," *Journal of Economic Perspectives* 25(4): 165-190. (optional)

Piketty, Thomas, and Emmanuel Saez (2013) "Optimal Labor Income Taxation," *Handbook of Public Economics*, Volume 5, Amsterdam: Elsevier-North Holland.

Saez, Emmanuel (2002) "Optimal Income Transfer Programs: Intensive versus Extensive Labor Supply Responses," *The Quarterly Journal of Economics* 117(3): 1039-1073. (optional)

September 23: Taxes and Labor Supply

Stantcheva

Gruber, Chapter 21

Chetty, R., J. Friedman and E. Saez (2013) "Using Differences in Knowledge Across Neighborhoods to Uncover the Impacts of the EITC on Earnings," *American Economic Review* 103(7): 2683-2721. (optional)

Eissa, N. and J. Liebman (1996) "Labor Supply Response to the Earned Income Tax Credit," *The Quarterly Journal of Economics* 111: 605-637. (optional)

Saez, E. "Do Taxpayers Bunch at Kink Points?" (2010) *American Economic Journal: Economic Policy*, 2: 180-212. (optional)

Pencavel, J. (1986) "Labor Supply of Men: A Survey," *Handbook of Labor Economics*, Volume 1, Chapter 1. (optional)

Heckman, J. and M. Killingsworth (1986) "Female Labor Supply: A Survey," *Handbook of Labor Economics*, Volume 1, Chapter 2. (optional)

September 25: Taxes and Reported Income

Stantcheva

Saez, Emmanuel, Joel Slemrod, and Seth H. Giertz (2012) “The Elasticity of Taxable Income with Respect to Marginal Tax Rates: A Critical Review,” *Journal of Economic Literature* 50(1): 3-50. (optional)

Piketty, Thomas, Emmanuel Saez, and Stefanie Stantcheva (2014) “Optimal Taxation of Top Labor Incomes: A Tale of Three Elasticities,” *American Economic Journal: Economic Policy*, 6(1). (optional)

Akcigit, Ufuk, Salomé Baslandze, and Stefanie Stantcheva (2016) “Taxation and the International Mobility of Inventors,” *American Economic Review* 106 (10): 2930–2981. (optional)

Goolsbee, Austan (2000) “What Happens When You Tax the Rich? Evidence from Executive Compensation,” *Journal of Political Economy* 108: 352-378. (optional)

October 2: Externalities

Stantcheva

Gruber, Chapter 5 and 6

Gruber, Jonathan (2001) “Tobacco at the Crossroads: The Past and Future of Smoking Regulation in the United States,” *Journal of Economic Perspectives* 15(2): 193-212. (optional)

Nordhaus, William D. (2006) “After Kyoto: Alternative Mechanisms to Control Global Warming,” *American Economic Review* 96(2): 31- 34. (optional)

October 7: Public Goods

Stantcheva

Gruber, Chapter 1 and 7

October 11: Social Insurance (Intro) and Health Insurance (Part I)

Stantcheva

Gruber, Chapter 12, 15, and 16

Case, Anne and Angus Deaton (2017) “Mortality and Morbidity in the 21st Century,” *Brookings Papers in Economic Activity*. (optional)

Currie, Janet, and Jonathan Gruber (1997) “The Technology of Birth: Health Insurance, Medical Interventions, and Infant Health,” *NBER Working Paper* 5985. (optional)

Finkelstein, Amy, Sarah Taubman, Bill Wright, Mira Bernstein, Jonathan Gruber, Joseph P. Newhouse, Heidi Allen, and Katherine Baicker (2012) “The Oregon Health Insurance Experiment: Evidence from the First Year,” *The Quarterly Journal of Economics* 127(3): 1057-1106. (optional)

Einav, Liran, Amy Finkelstein, and Paul Schrimpf (2013) “The Response of Drug Expenditures to Nonlinear Contract Design: Evidence from Medicare Part D,” *NBER Working Paper* 19393. (optional)

October 16: The Federal Budget

Veuger

Gruber, Chapter 4

Congressional Budget Office. *The 2019 Long-Term Budget Outlook*. June 2019.

W.G. Gale (2019) “Government at a Glance.” In: *Fiscal Therapy: Curing America’s Debt Addiction and Investing in the Future*. New York, NY: Oxford University Press. 17-32.

Capretta, James C. (2019) “The Congressional Budget Process: A Brief Primer,” *AEI Economic Perspectives* 2018-02 (February). (optional)

October 21: Health Insurance (Part II)

Stantcheva

Gruber, Chapter 15 and 16

Case, Anne and Angus Deaton (2017) “Mortality and Morbidity in the 21st Century,” *Brookings Papers in Economic Activity*. (optional)

Currie, Janet, and Jonathan Gruber (1997) “The Technology of Birth: Health Insurance, Medical Interventions, and Infant Health,” *NBER Working Paper* 5985. (optional)

Finkelstein, Amy, Sarah Taubman, Bill Wright, Mira Bernstein, Jonathan Gruber, Joseph P. Newhouse, Heidi Allen, and Katherine Baicker (2012) “The Oregon Health Insurance Experiment: Evidence from the First Year,” *The Quarterly Journal of Economics* 127(3): 1057-1106. (optional)

Einav, Liran, Amy Finkelstein, and Paul Schrimpf (2013) “The Response of Drug Expenditures to Nonlinear Contract Design: Evidence from Medicare Part D,” *NBER Working Paper* 19393. (optional)

October 25: Social Security

Veuger

Gruber, Chapter 13

Martin Feldstein, “Structural Reform of Social Security,” *Journal of Economic Perspectives*, Spring 2005, pp 33-55.

Martin Feldstein and Jeffrey Liebman, “The Distributional Effects of an Investment Based Social Security System,” in Martin Feldstein and Jeffrey Liebman, eds., *The*

Distributional Aspects of Social Security and Social Security Reform, Chicago: University of Chicago Press, 2002, 263-326. (optional)

Coile, Courtney, Kevin S. Milligan, and David A. Wise (2016) “Health Capacity to Work at Older Ages: Evidence from the U.S.” *NBER Working Paper* No. 21940. (optional)

James M. Poterba, Steven F. Venti and David A. Wise (1996) “How Retirement Savings Programs Increase Saving,” *Journal of Economic Perspectives* 10(4): 91-112. (optional)

Eric M. Engen, William G. Gale, and John Karl Scholz (1996) “The Illusory Effects of Savings Incentives,” *Journal of Economic Perspectives* 10(4): 113-138. (optional)

Biggs, Andrew G., and Sylvester Schieber (2014) “Is There a Retirement Crisis?” *National Affairs*. Summer.

Beshears, John, James J. Choi, David Laibson, Brigitte C. Madrian, William L. Skimmyhorn (2019) “Borrowing to Save? The Impact of Automatic Enrollment on Debt,” *NBER Working Paper* No. 25876. (optional)

October 28: Tax Reform

Veuger

Gruber, Chapter 25

Martin Feldstein (2011) “Tax Reform: Evidence of 1986,” *The Wall Street Journal*, October 14. (optional)

Elmendorf, Douglas (2015) “‘Dynamic Scoring’: Why and How to Include Macroeconomic Effects in Budget Estimates for Legislative Proposals,” *Brookings Papers on Economic Activity*, Fall. (optional)

Martin Feldstein (2015) “Raising Revenue by Limiting Tax Expenditures,” *Tax Policy and the Economy*, Vol. 29. (optional)

PwC Washington National Tax Services (2017) “Congress Gives Final Approval to Tax Reform Conference Committee Agreement,” *Tax Insight*, December 2017. (optional)

R. Barro and J. Furman (2018) “The Macroeconomic Effects of the 2017 Tax Reform,” *Brookings Papers on Economic Activity*, Spring.

Veuger, Stan (2018) “8 Ways to Improve the Tax Code,” *National Interest*, January 5.

Brill, Alex, and Choe, Derrick (2018) “Charitable Giving and the Tax Cuts and Jobs Act,” *AEI Economic Perspectives* 2018-06 (June). (optional)

Veuger, Stan (2019) “Modern Monetary Theory and Policy,” *AEI Economic Perspectives* 2019-01a. (optional)

Gruber, Chapter 24 (optional)

Saul Levmore and Hideki Kanda (1991) "Taxes, Agency Costs, and the Price of Incorporation," *Virginia Law Review* 77: 211-256.

Raj Chetty and Emmanuel Saez (2005) "Dividend Taxes and Corporate Behavior: Evidence from the 2003 Dividend Tax Cut," *Quarterly Journal of Economics* 120(3): 791–833. (optional)

Danny Yagan (2015) "Capital Tax Reform and the Real Economy: The Effects of the 2003 Dividend Tax Cut," *American Economic Review* 105(12) pp. 3531-3563.

J. C. Suárez Serrato and O. Zidar (2016) "Who Benefits from State Corporate Tax Cuts? A Local Labor Markets Approach with Heterogeneous Firms," *American Economic Review* 106(9): 2582-2624. (optional)

PwC Washington National Tax Services (2017) "Congress Gives Final Approval to Tax Reform Conference Committee Agreement," *Tax Insight*, December 2017. (optional)

Gruber, Chapter 9

Downs, Anthony (1957). "An Economic Theory of Political Action in a Democracy," *Journal of Political Economy* 65(2): 135–150. (optional)

Madestam, Andreas, Daniel Shoag, Stan Veuger, and David Yanagizawa-Drott (2013) "Do Political Protests Matter? Evidence from the Tea Party Movement," *Quarterly Journal of Economics* 128(4): 1633-1685.

Baker, Scott R., Nicholas Bloom, and Steven J. Davis (2016) "Measuring Economic Policy Uncertainty," *Quarterly Journal of Economics* 131(4): 1593–1636.

Alesina, Alberto and Nouriel Roubini (1992) "Political Cycles in OECD Economies" *Review of Economic Studies* 59(4): 663-688. (optional)

Stephens-Davidowitz, Seth (2014) "The Cost of Racial Animus on a Black Candidate: Evidence using Google Search Data," *Journal of Public Economics* 118: 26-40. (optional)

Chapter 5 and 8

Weitzman, Martin L. (1974) "Prices vs. Quantities," *Review of Economic Studies* 41(4): 477-491. (optional)

Summers, Lawrence (1989) "Some Simple Economics of Mandated Benefits," *American Economic Review* 79(2): 177-183.

Gruber, Jonathan (1994) "The Incidence of Mandated Maternity Benefits," *American Economic Review* 84(3): 622-641.

Clemens, Jeffrey (2008) "Opium in Afghanistan: Prospects for the Success of Source Country Drug Control Policies," *Journal of Law and Economics* 51(3): 407-432. (optional)

Cicala, Steve (2015) "When Does Regulation Distort Costs? Lessons from Fuel Procurement in US Electricity Generation," *American Economic Review* 105(1): 411-444. (optional)

Clemens, Jeffrey, and Michael Wither (2019) "The Minimum Wage and the Great Recession: Evidence of Effects on the Employment and Income Trajectories of Low-Skilled Workers," *Journal of Public Economics* 170: 53-67. (optional)

Clemens, Jeffrey (2019) "Making Sense of the Minimum Wage: A Roadmap for Navigating Recent Research," *Cato Institute Policy Analysis* No. 867.

Shoag, Daniel, and Veuger, Stan (2019) "'Ban the Box' Measures Help High-Crime Neighborhoods," Mimeo: Case Western Reserve University and American Enterprise Institute. (optional)

November 18 and 20: Multilevel Government

Veuger

Gruber, Chapter 10 and 11

Blanchard, Olivier J., and Lawrence F. Katz, "Regional Evolutions," *Brookings Papers on Economic Activity*, no. 1 (1992). (optional)

Davis, Donald R., and David E. Weinstein, "Bones, Bombs, and Break Points: The Geography of Economic Activity," *American Economic Review* 92, no. 5 (2002), 1269-1289.

Tiebout, Charles (1956) "A Pure Theory of Local Expenditures," *Journal of Political Economy* 64(5): 416-424. (optional)

Hoxby, Caroline (2000) "Does Competition among Public Schools Benefit Students and Taxpayers?" *American Economic Review* 90(5): 1209-1238. (optional)

Ganong, Peter, and Daniel Shoag (2017) "Why Has Regional Income Convergence in the U.S. Declined?" *Journal of Urban Economics* 102 (November): 76-90.

Glaeser, Edward L., and Joseph Gyourko, "Urban Decline and Durable Housing" *Journal of Political Economy* 113, no. 2 (2005), 345-375. (optional)

Shoag, Daniel, and Stan Veuger (2018) "Shops and the City: Evidence on Local Externalities and Local Government Policy from Big-Box Bankruptcies," *Review of Economics and Statistics* 100(3): 440-453.

Shoag, Daniel, Cody Tuttle, and Stan Veuger (2019) "Rules versus Home Rule: Local Government Responses to Negative Revenue Shocks," *National Tax Journal* 72(3): 543-574. (optional)

November 25: Health Care Reform

Veuger

Gruber, Chapter 15 and 16 (optional)

Congressional Budget Office. *The 2019 Long-Term Budget Outlook*. June 2019.

Blahous, Charles (2019) "The Unanswered Questions for Medicare for All," *AEI Economic Perspectives* 2019-02 (February).

Holahan, John, and Linda J. Blumberg (2018) *Estimating the Cost of a Single-Payer Plan*. Urban Institute Health Policy Center.

Clemens, Jeffrey, and Joshua Gottlieb (2014) "Do Physicians' Financial Incentives Affect Treatment Patterns and Patient Health?" *American Economic Review* 104(4): 1320-1349. (optional)

Clemens, Jeffrey (2015) "Regulatory Redistribution in the Market for Health Insurance," *American Economic Journal: Applied Economics* 7(2): 109-134. (optional)

Clemens, Jeffrey, and Joshua Gottlieb (2017) "In the Shadow of a Giant: Medicare's Influence on Private Payment Systems," *Journal of Political Economy* 125(1): 1-39.

December 2: Unemployment & Disability Insurance, Workers' Compensation

Stantcheva

Gruber, Chapter 14

Bound, John (1989) "The Health and Earnings of Rejected Disability Insurance Applicants," *American Economic Review* 79(3): 482-503. (optional)

Card, David, Raj Chetty, and Andrea Weber (2007) "The Spike at Benefit Exhaustion: Leaving the Unemployment System or Starting a New Job?" *American Economic Review* 97(2): 113-118. (optional)

Gruber, Jonathan (1997) "The Consumption Smoothing Benefits of Unemployment Insurance," *American Economic Review*. (optional)