Correction: “Local Projections and VARs Estimate the Same Impulse Responses”

Mikkel Plagborg-Møller   Christian K. Wolf

October 14, 2021

In Example 2 (pp. 967–968) of Plagborg-Møller and Wolf (2021) appears the following erroneous statement:

To estimate relative impulse responses $\Theta_{1,2,h}/\Theta_{1,2,0}$ to the demand shock, the researcher can choose any vector $\tilde{b}$ such that $\tilde{b}'b = 0$, and then implement the local projection (9) with $\tilde{b}$ in lieu of $b$.

The correct statement is:

To estimate relative impulse responses $\Theta_{1,2,h}/\Theta_{1,2,0}$ to the demand shock, the researcher can choose any vector $\tilde{b}$ such that $\tilde{b}'\text{Var}(w_t | \{w_{\tau}\}_{-\infty<\tau<t})b = 0$, and then implement the local projection (9) with $\tilde{b}$ in lieu of $b$.

The above condition ensures that the demand shock $\tilde{b}'u_t$ is orthogonal to the previously identified supply shock $b'u_t$, where $u_t \equiv w_t - E(w_t | \{w_{\tau}\}_{-\infty<\tau<t})$.

We are grateful to Gabriel Chodorow-Reich for bringing this typo to our attention.

References