
BOOK REVIEWS



Mark Kritzman, Senior Editor

EMPIRICAL DYNAMIC ASSET PRICING: MODEL SPECIFICATION AND ECONOMETRIC ASSESSMENT

By Kenneth J. Singleton

(Reviewed by Cel Kulasekaran)

Kenneth Singleton has written an outstanding book about the construction and empirical testing of asset pricing models. He presents the theoretical and empirical framework for econometric methods, estimation of discrete-time asset pricing models, and no-arbitrage continuous-time dynamic asset pricing models in three distinct sections of the book. His presentation is orderly and methodical, making it easier to digest the content which at times may seem quite complex and dense.

The first few chapters of the book formally introduce the necessary ingredients required to set up and

work with dynamic asset pricing models. Singleton expediently divulges assumptions and restrictions along with estimators used in pricing theory. He discusses foundational work in mathematical statistics such as the generalized method of moments, maximum likelihood methods, and quasi-maximum likelihood estimators as preparation for the following sections of the book. Those who are conversant with these topics may choose to skip most of the first few chapters, but should review the chapters which discuss affine processes and stochastic volatility and jumps, as these are crucial background material for future sections.

In the second part of the book, Singleton provides a masterful discussion on pricing kernels, consumption, and factor-models. He begins by introducing the notion of pricing kernels, carefully extending the

theory from the first part of the book, and extends this concept to its relationship with marginal rates of consumption and risk-neutral pricing. Next, he thoroughly discusses the economic motivation behind asset return predictability and offers empirical support from studies of equity and fixed-income markets. While exploring the restrictions and implications of linear asset pricing models, Singleton also includes an extensive review of literature and work-in-progress about serial-correlation of returns. The section ends with an overview of preference-based and factor models, in which he addresses the goodness-of-fit of these models.

In the third part, Singleton reviews the current literature on no-arbitrage dynamic asset pricing models focusing on continuous-time models. In my

view, standard asset pricing texts do not usually cover this topic very well. He devotes the first two chapters of this section to dynamic term structure models for market yields on default-free bonds, and he follows up with empirical analyses. He discusses at length key models such as affine quadratic Gaussian models, non-affine stochastic volatility models, and regime shift models. He similarly discusses defaultable bonds. The final two chapters of the book explore pricing models for equity and fixed-income derivatives.

I particularly appreciated Singleton's discussion of the assumptions and restrictions behind the various models he reviews. The book also benefits from Singleton's excellent review of the sizable literature on the subjects, especially many updated empirical experiments. Experienced practitioners who seek a detailed review of the subject will find Singleton's book very appealing. Even determined initiates with a sense of adventure will benefit from Singleton's excellent presentation of this highly technical material. The bottom line is that whether you are an initiate or experienced practitioner, Singleton's book deserves space on your shelf.

CONFESSIONS OF AN ECONOMIC HIT MAN

*By John Perkins
(Reviewed by Tim Adler)*

Confessions of an Economic Hit Man is a narration by John Perkins of his life story and 20-year career working for a Boston based global consulting firm.

Central to the book is an examination of Economic Hit Men (EHM) and the role they play in a global conspiracy to gain wealth and power for America and her allies. By Perkins' own claim he was an excellent EHM.

An EHM develops inflated economic projection models to justify massive engineering and construction projects in developing countries. The projects are typically financed with loans provided by the US government and other affiliated aid organizations,¹ and the construction contracts are awarded to US construction firms to ensure that the money never leaves the US economy.

When the inflated economic forecasts fail to materialize and the developing country has difficulty in meeting repayments, the United States as creditor exploits this situation to ensure favorable responses to requests for military

bases, access to natural resources, and political support.

The book proceeds chronologically. Chapter 2 recounts Perkins' indoctrination and training to become an EHM. Chapters 3 through 9 describe in detail his first EHM assignment in Indonesia, in which his task was to develop inflated electricity demand forecasts. Chapters 10 through 13 recount his next assignment in Panama where maintaining US control of the Panama Canal was an EHM priority.

Chapter 15 contains a fascinating account of the use of EHM as part of the US response to the 1973 oil embargo. Realizing the vulnerability of the US economy to Middle East oil shocks, the United States sought to develop a strategic partnership with Saudi Arabia. The partnership, known as JECOR,² used American EHM, technology and expertise to modernize the Saudi military and civilian infrastructure. In addition, Washington offered the House of Saudi political and military support to maintain their grip on power. In exchange the Saudis guaranteed there would not be another oil embargo and agreed to invest the proceeds of oil sales in US government securities.

The two countries further agreed that the interest payments otherwise due to Saudi Arabia would instead be diverted to JECOR, to pay for the modernization of Saudi Arabia, which was under the direct control of the US Treasury department. Perkins explains: "In other words, the interest compounding on billions of dollars of the kingdom's oil income would be used to pay US companies to fulfill the vision I (and presumably some of my competitors) had come up with . . . Our own U.S. Department of the Treasury would hire us, at Saudi expense, to build infrastructure projects and even entire cities throughout the Arabian Peninsula."³

The remainder of the book chronicles his experiences in Iran and Ecuador, his transition away from consulting, and finally his retirement.

While the book is engaging and well worth reading, I offer two cautionary comments. In spite of the title, Perkins overlooks obvious opportunities to "confess" fully by providing details of

his EHM activities. This detracts from his credibility and undermines his thinly disguised goal of receiving absolution for his "sins." Instead he is often prone to self-serving introspection and hollow, *posteriori* justifications for actions.

Also, in several instances the book makes sensational claims with weak supporting evidence. For example, Perkins asserts he was recruited by the NSA⁴ and that they provided career guidance. The only account of interaction with the NSA, however, does not have enough weight to support this claim. In Chapter 1, Perkins provides an account of an interview he had with a senior NSA officer and family friend, Frank, when he was nearing completion of his undergraduate degree. At the conclusion of the interview process Perkins was offered a job with the NSA, but he declined this and instead joined the Peace Corps with Frank's agreement. He concluded from this interaction that Frank and the NSA covertly monitored and supported his career.

I whole heartedly recommend the book to readers on the basis of wetting one's appetite for a further consideration of the important topics raised. If readers overlook the liberties the author has taken in telling his story they will be rewarded with an informative and at times provocative account of American corporate history Post Second World War.

Notes

- ¹ Page 17. All page references refer to the Plume January 2006 paperback edition.
- ² United States – Saudi Arabian Joint Economic Commission.
- ³ Page 103.
- ⁴ Page 160.

Book Review Correction

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Frank Jones reviewed "The Nobel Memorial Laureates in Economics: An Introduction to their Careers and Main Published Works, 2005, by Howard R. Vane and Chris Mulhearn