

William C. Brainard

William C. Brainard is the Arthur Okun Professor Emeritus of Economics at Yale University. He is an economic theorist who works on monetary policy, the market valuation of firms and models of financial markets. He was the co-author of a paper that introduced a landmark innovation in investment theory, linking real and financial markets. In “Pitfalls in Financial Model Building”, *American Economic Review* (1968), Brainard and Tobin introduced the idea that a firm’s investment should be positively related to the ratio of its market value to the replacement value of its capital stock, though they did not use the letter “Q” to denote this ratio. James Tobin’s *JMCB paper*, “A General Equilibrium Approach to Monetary Policy” (1969), went on to use the notation “Q” for the same concept. Tobin’s Q, as it has become known, is the implementation of Keynes’s *The General Theory of Employment, Interest and Money* (1936) notion that capital investment becomes more attractive as the value of capital increases relative to the cost of acquiring the capital. Lucas and Prescott’s 1971 *Econometrica* paper, “Investment under Uncertainty” developed a rigorous analysis of the capital investment decision in the presence of convex costs of adjustment, and observed that the market value of capital can be an important element of the capital investment decision. Tobin’s Q, which originated with Brainard and Tobin’s *AER* piece, became a central theory of investment. Brainard, Shoven and Weiss’s “The Financial Valuation of the Return to Capital” (1980) is an empirical investigation of Q, concentrating on the alternative explanations for the huge fall in the market valuation of capital relative to its replace cost in the 1970s. Individual firm data was used to sort through the various hypotheses attempting to explain the low valuations. One simple explanation that could not be rejected was that investors were using high nominal interest rates to discount real risk adjusted cash flows rather than the more appropriate real interest rates. This idea was referred to as “inflation confusion.” The paper was part of a large literature on the excess volatility of financial markets relative to underlying dividends or cash flows.

William Brainard has been a major input into the research of graduate students and faculty alike at Yale for almost fifty years. Bill Nordhaus of Yale affectionately refers to Brainard as the kibitzer-in-chief as he is willing to exchange ideas with anybody and everybody. His breadth of knowledge and ability to get to the essence of a problem make him invaluable in seminars. This talent was put to exceptional use in his 27-year term as co-editor of the *Brookings Papers on Economic Activity*, from 1980 to 2007. In that context, he matched important topics with talented authors and had significant impact on the resulting papers for more than a generation. Bill did more than his share of administrative service at Yale, twice serving as Director of the Cowles Foundation for Research in Economics, as Chair of the Economics Department, and as Provost of the University (from 1981-86). William Brainard would be a most deserving Distinguished Fellow of the American Economics Association.