Investment Networks, Sectoral Comovement, and the Changing U.S. Business Cycle

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We study the role of sectoral comovement in accounting for changes in the U.S. business cycle since the 1980s. We first show that the correlation of value added across sectors has fallen since the 1980s but that the correlation of employment has not. These patterns statistically account for the decline in both GDP volatility and the cyclicality of labor productivity since the 1980s. We then build a model with sectoral linkages in both final and investment goods. The model endogenously matches the observed changes in sectoral comovement patterns, driven by the change in the covariance matrix of sectoral TFP shocks. The structure of the investment network is key to generating this result because it propagates sectoral shocks across sectors more strongly for employment than value added. Our calibrated model accounts for a significant portion of the changes in aggregate fluctuations since the 1980s.