
grmpy Documentation

Release 1.0

Development Team

Jul 16, 2018

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[PyPI](#) | [GitHub](#) | [Issues](#)

`grmpy` is an open-source Python package for the simulation and estimation of the generalized Roy model. It serves as a teaching tool to promote the conceptual framework of the generalized Roy model, illustrate a variety of issues in the econometrics of policy evaluation, and showcase basic software engineering practices.

We build on the following main references:

James J. Heckman and Edward J. Vytlačil. [Chapter 70 Econometric Evaluation of Social Programs, Part I: Causal Models, Structural Models and Econometric Policy Evaluation](#). Handbook of Econometrics, 6, 4779 – 4874, 2007.

James J. Heckman and Edward J. Vytlačil. [Chapter 71 Econometric Evaluation of Social Programs, Part II: Using the Marginal Treatment Effect to Organize Alternative Econometric Estimators to Evaluate Social Programs, and to Forecast their Effects in New Environments](#). Handbook of Econometrics, 6, 4875 – 5143, 2007.

Contents:

This section provides a general discussion of the generalized Roy model and selected issues in the econometrics of policy evaluation. The `grmpy` package implements a parametric normal version of the model, please see the next section for details.

1.1 Generalized Roy Model

The generalized Roy model (Roy, 1951 [23]; Heckman and Vytlacil, 2005 [11]) provides a coherent framework to explore the econometrics of policy evaluation. Its parametric version is characterized by the following set of equations.

Potential Outcomes

$$Y_1 = \mu_1(X) + U_1$$

$$Y_0 = \mu_0(X) + U_0$$

Choice

$$D = I[S > 0]$$

$$S = E[Y_1 - Y_0 - C \mid \mathcal{I}]$$

$$C = \mu_C(Z) + U_C$$

Observed Outcome

$$Y = DY_1 + (1 - D)Y_0$$

(Y_1, Y_0) are objective outcomes associated with each potential treatment state D and realized after the treatment decision. Y_1 refers to the outcome in the treated state and Y_0 in the untreated state. C denotes the subjective cost of treatment participation. Any subjective benefits, e.g. job amenities, are included (as a negative contribution) in the subjective cost of treatment. Agents take up treatment D if they expect the objective benefit to outweigh the subjective cost. In that case, their subjective evaluation, i.e. the expected surplus from participation S , is positive. I denotes the agent's information set at the time of the participation decision. The observed outcome Y is determined in a switching-regime fashion (Quandt 1958 [20], 1972 [21]). If agents take up treatment, then the observed outcome Y corresponds to the outcome in the presence of treatment Y_1 . Otherwise, Y_0 is observed. The unobserved potential outcome is referred to as the counterfactual outcome. If costs are identically zero for all agents, there are no observed regressors, and $(U_1, U_0) \sim N(0, \Sigma)$, then the generalized Roy model corresponds to the original Roy model (Roy, 1951 [23]).

From the perspective of the econometrician, (X, Z) are observable while (U_1, U_0, U_C) are not. X are the observed determinants of potential outcomes (Y_1, Y_0) , and Z are the observed determinants of the cost of treatment C . Potential outcomes and cost are decomposed into their means $(\mu_1(X), \mu_0(X), \mu_C(Z))$ and their deviations from the mean (U_1, U_0, U_C) . (X, Z) might have common elements. Observables and unobservables jointly determine program participation D .

If their ex ante surplus S from participation is positive, then agents select into treatment. Yet, this does not require their expected objective returns to be positive as well. Subjective cost C might be negative such that agents which expect negative returns still participate. Moreover, in the case of imperfect information, an agent's ex ante evaluation of treatment is potentially different from their ex post assessment.

The evaluation problem arises because either Y_1 or Y_0 is observed. Thus, the effect of treatment cannot be determined on an individual level. If the treatment choice D depends on the potential outcomes, then there is also a selection problem. If that is the case, then the treated and untreated differ not only in their treatment status but in other characteristics as well. A naive comparison of the treated and untreated leads to misleading conclusions. Jointly, the evaluation and selection problem are the two fundamental problems of causal inference (Holland, 1986 [16]).

1.2 Selected Issues

We now highlight some selected issues in the econometrics of policy evaluation that can be fruitfully discussed within the framework of the model.

1.2.1 Agent Heterogeneity

What gives rise to variation in choices and outcomes among, from the econometrician's perspective, otherwise observationally identical agents? This is the central question in all econometric policy analyses (Browning et al., 1999 [4]; Heckman, 2001 [7]).

The individual benefit of treatment is defined as

$$B = Y_1 - Y_0 = (\mu_1(X) - \mu_0(X)) + (U_1 - U_0).$$

From the perspective of the econometrician, differences in benefits are the result of variation in observable X and unobservable characteristics $(U_1 - U_0)$. However, $(U_1 - U_0)$ might be (at least partly) included in the agent's information set I and thus known to the agent at the time of the treatment decision.

As a result, unobservable treatment effect heterogeneity can be distinguished into private information and uncertainty. Private information is only known to the agent but not the econometrician; uncertainty refers to variability that is unpredictable by both.

The information available to the econometrician and the agent determines the set of valid estimation approaches for the evaluation of a policy. The concept of essential heterogeneity emphasizes this point (Heckman et al., 2006 [15]).

1.2.2 Essential Heterogeneity

If agents select their treatment status based on benefits unobserved by the econometrician (selection on unobservables), then there is no unique effect of a treatment or a policy even after conditioning on observable characteristics. Average benefits are different from marginal benefits, and different policies select individuals at different margins. Conventional econometric methods that only account for selection on observables, like matching (Cochran and Rubin, 1973 [5]; Rosenbaum and Rubin 1983 [22] ; Heckman et al., 1998 [9]), are not able to identify any parameter of interest (Heckman and Vytlačil, 2005 [11]; Heckman et al., 2006 [15]).

1.3 Objects of Interest

Treatment effect heterogeneity requires to be precise about the effect being discussed. There is no single effect of neither a policy nor a treatment. For each specific policy question, the object of interest must be carefully defined (Heckman and Vytlačil, 2005 [11], 2007a [12],b [13]). We present several potential objects of interest and discuss what question they are suited to answer. We start with the average effect parameters. However, these neglect possible effect heterogeneity. Therefore, we explore their distributional counterparts as well.

1.3.1 Conventional Average Treatment Effects

It is common to summarize the average benefits of treatment for different subsets of the population. In general, the focus is on the average effect in the whole population, the average treatment effect (ATE), or the average effect on the treated (TT) or untreated (TUT).

$$\begin{aligned}ATE &= E[Y_1 - Y_0] \\ TT &= E[Y_1 - Y_0 | D = 1] \\ TUT &= E[Y_1 - Y_0 | D = 0]\end{aligned}$$

The relationship between these parameters depends on the assignment mechanism that matches agents to treatment. If agents select their treatment status based on their own benefits, then agents that take up treatment benefit more than those that do not and thus $TT > TUT$. If agents select their treatment status at random, then all parameters are equal. The policy relevance of the conventional treatment effect parameters is limited. They are only informative about extreme policy alternatives. The ATE is of interest to policy makers if they weigh the possibility of moving a full economy from a baseline to an alternative state or are able to assign agents to treatment at random. The TT is informative if the complete elimination of a program already in place is considered. Conversely, if the same program is examined for compulsory participation, then the TUT is the policy relevant parameter. To ensure a tight link between the posed policy question and the parameter of interest, Heckman and Vytlacil (2001 [10]) propose the policy-relevant treatment effect (PRTE). They consider policies that do not change potential outcomes, but only affect individual choices. Thus, they account for voluntary program participation. Policy-Relevant Average Treatment Effects The PRTE captures the average change in outcomes per net person shifted by a change from a baseline state B to an alternative policy A . Let D_B and D_A denote the choice taken under the baseline and the alternative policy regime respectively. Then, observed outcomes are determined as

$$\begin{aligned}Y_B &= D_B Y_1 + (1 - D_B) Y_0 \\ Y_A &= D_A Y_1 + (1 - D_A) Y_0.\end{aligned}$$

A policy change induces some agents to change their treatment status ($D_B \neq D_A$), while others are unaffected. More formally, the PRTE is then defined as

$$PRTE = E[D_A] - E[D_B](E[Y_A] - E[Y_B]).$$

In our empirical illustration, in which we consider education policies, the lack of policy relevance of the conventional effect parameters is particularly evident. Rather than directly assigning individuals a certain level of education, policy makers can only indirectly affect schooling choices, e.g. by altering tuition cost through subsidies. The individuals drawn into treatment by such a policy will neither be a random sample of the whole population, nor the whole population of the previously (un-)treated. That is why we estimate the policy-relevant effects of alternative education policies and contrast them with the conventional treatment effect parameters. We also show how the PRTE varies for alternative policy proposals as different agents are induced to change their treatment status.

1.3.2 Local Average Treatment Effect

The Local Average Treatment Effect (LATE) was introduced by Imbens and Angrist (1994 [19]). They show that instrumental variable estimator identify LATE, which measures the mean gross return to treatment for individuals induced into treatment by a change in an instrument.

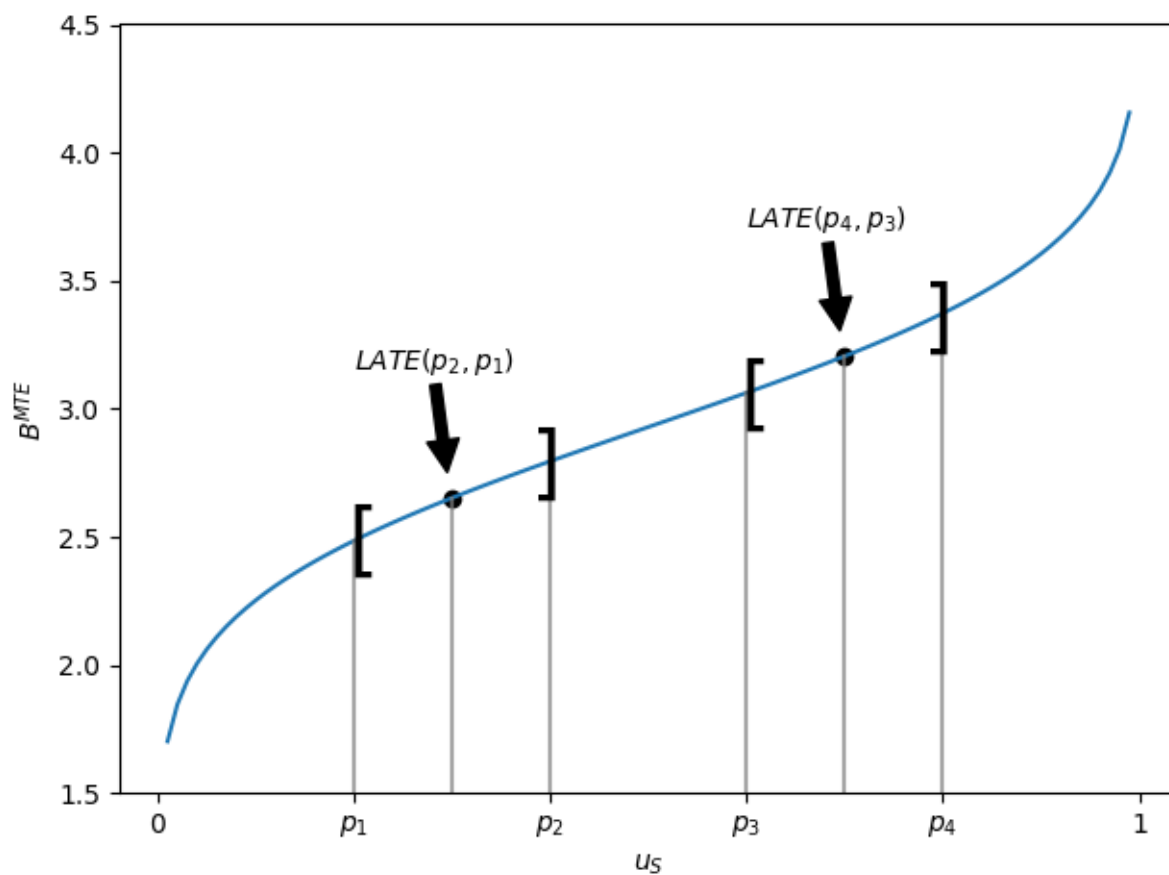


Fig. 1: LATE at different values of u_S

Unfortunately, the people induced to go into state 1 ($D = 1$) by a change in any particular instrument need not to be the same as the people induced to go to state 1 by policy changes other than those corresponding exactly to the variation in the instrument. A desired policy effect may not be directly correspond to the variation in the IV. Moreover, if there is a vector of instruments that generates choice and the components of the vector are intercorrelated, IV estimates using the components of Z as the instruments, one at a time, do not, in general, identify the policy effect corresponding to varying that instruments, keeping all other instruments fixed, the *ceteris paribus* effect of the change in the instrument. Heckman develops this argument in detail (2010 [8]).

The average effect of a policy and the average effect of a treatment are linked by the marginal treatment effect (MTE). The MTE was introduced into the literature by Björklund and Moffitt (1987 [3]) and extended in Heckman and Vytlacil (2001 [10], 2005 [11], 2007b [13]).

1.3.3 Marginal Treatment Effect

The MTE is the treatment effect parameter that conditions on the unobserved desire to select into treatment. Let $V = E[U_C - (U_1 - U_0)|I]$ summarize the expectations about all unobservables determining treatment choice and let $U_S = F_V(V)$. Then, the MTE is defined as

$$MTE(x, u_S) = E[Y_1 - Y_0 | X = x, U_S = u_S].$$

The MTE is the average benefit for persons with observable characteristics $X = x$ and unobservables $U_S = u_S$. By construction, U_S denotes the different quantiles of V . So, when varying U_S but keeping X fixed, then the MTE shows how the average benefit varies along the distribution of V . For u_S evaluation points close to zero, the MTE is the average effect of treatment for individuals with a value of V that makes them most likely to participate. The opposite is true for high values of u_S . The MTE provides the underlying structure for all average effect parameters previously discussed. These can be derived as weighted averages of the MTE (Heckman and Vytlacil, 2005 [11]).

Parameter j , $\Delta j(x)$, can be written as

$$\Delta j(x) = \int_0^1 MTE(x, u_S) h_j(x, u_S) du_S,$$

where the weights $h_j(x, u_S)$ are specific to parameter j , integrate to one, and can be constructed from data.

All parameters are identical only in the absence of essential heterogeneity. Then, the $MTE(x, u_S)$ is constant across the whole distribution of V as agents do not select their treatment status based on their unobservable benefits.

So far, we have only discussed average effect parameters. However, these conceal possible treatment effect heterogeneity, which provides important information about a treatment. Hence, we now present their distributional counterparts (Aakvik et al., 2005 [1]).

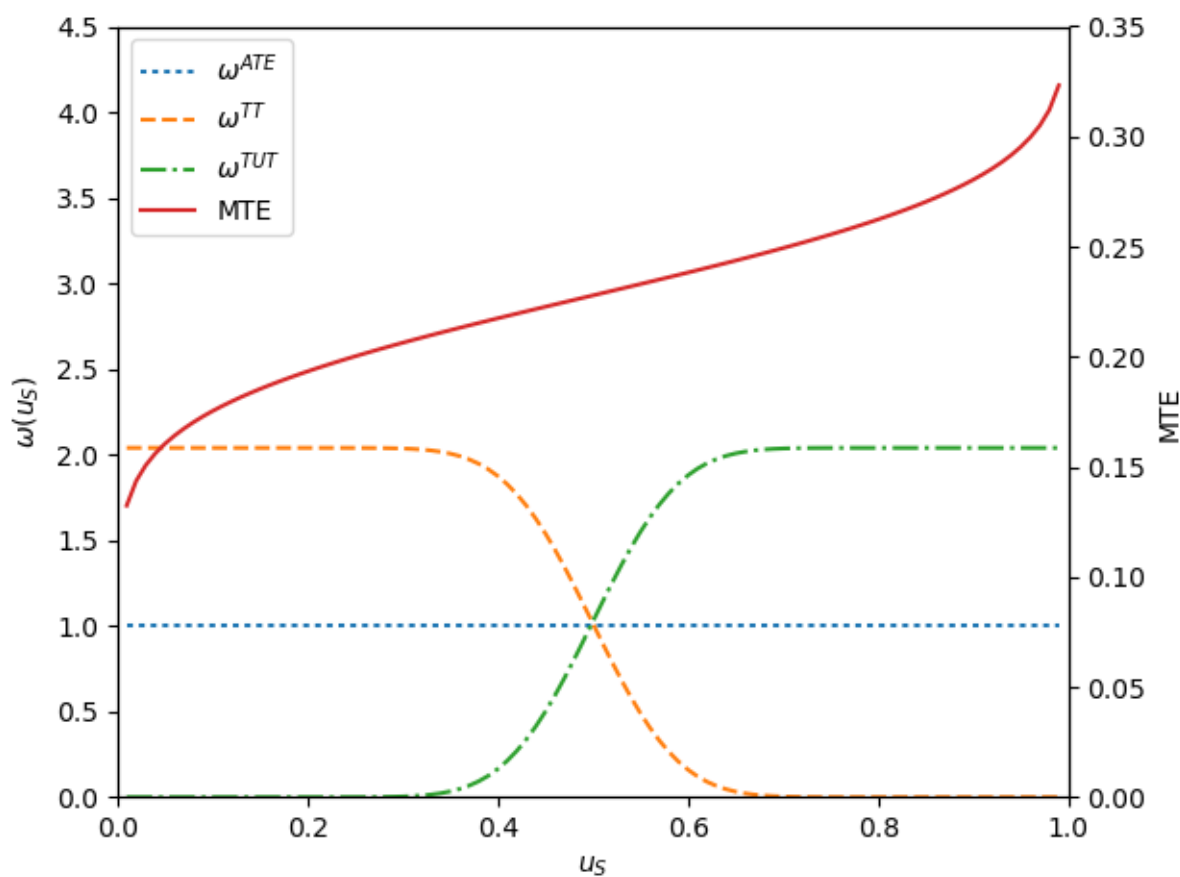


Fig. 2: Weights for the marginal treatment effect for different parameters.

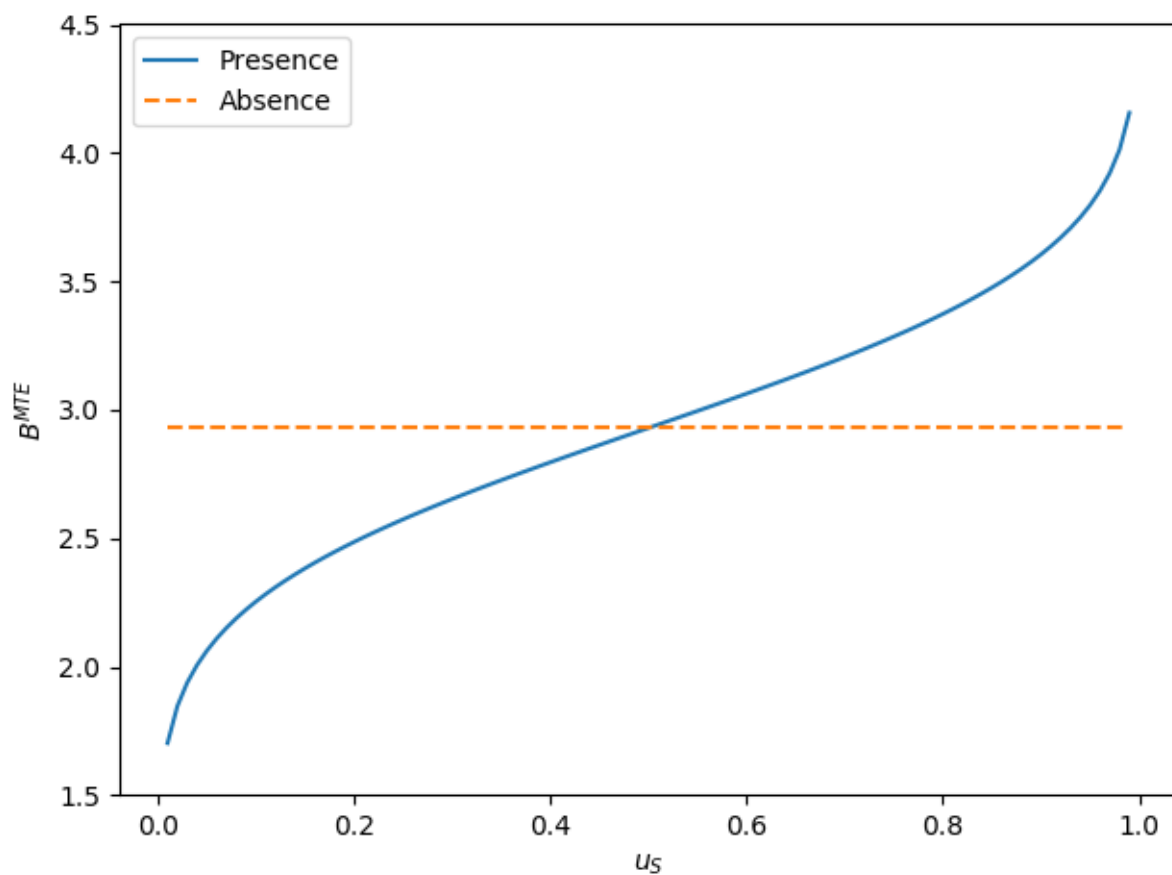


Fig. 3: MTE in the presence and absence of essential heterogeneity.

1.3.4 Distribution of Potential Outcomes

Several interesting aspects of policies cannot be evaluated without knowing the joint distribution of potential outcomes (see Abbring and Heckman, 2007 [2] and Heckman et al., 1997 [14]). The joint distribution of (Y_1, Y_0) allows to calculate the whole distribution of benefits. Based on it, the average treatment and policy effects can be constructed just as the median and all other quantiles. In addition, the portion of people that benefit from treatment can be calculated for the overall population $Pr(Y_1 - Y_0 > 0)$ or among any subgroup of particular interest to policy makers $Pr(Y_1 - Y_0 > 0|X)$. This is important as a treatment which is beneficial for agents on average can still be harmful for some. The absence of an average effect might be the result of part of the population having a positive effect, which is just offset by a negative effect on the rest of the population. This kind of treatment effect heterogeneity is informative as it provides the starting point for an adaptive research strategy that tries to understand the driving force behind these differences (Horwitz et al., 1996 [17], 1997 [18]).

CHAPTER 2

Installation

The `grmpy` package can be conveniently installed from the [Python Package Index \(PyPI\)](#) or directly from its source files. We currently support Python 2.7 and Python 3.6 on Linux systems.

2.1 Python Package Index

You can install the stable version of the package the usual way.

```
$ pip install grmpy
```

2.2 Source Files

You can download the sources directly from our [GitHub repository](#).

```
$ git clone https://github.com/grmToolbox/grmpy.git
```

Once you obtained a copy of the source files, installing the package in editable model is straightforward.

```
$ pip install -e .
```

2.3 Test Suite

Please make sure that the package is working properly by running our test suite using `pytest`.

```
$ python -c "import grmpy; grmpy.test()"
```

We now illustrate the basic capabilities of the `grmpy` package. We start with the assumptions about functional form and the distribution of unobservables and then turn to some simple use cases.

3.1 Assumptions

The `grmpy` package implements the normal linear-in-parameters version of the generalized Roy model. Both potential outcomes and the cost associated with treatment participations (Y_1, Y_0, C) are a linear function of the individual's observables (X, Z) and random components (U_1, U_0, U_C) .

$$Y_1 = X\beta_1 + U_1$$

$$Y_0 = X\beta_0 + U_0$$

$$C = Z\gamma + U_C$$

We collect all unobservables determining treatment choice in $V = U_C - (U_1 - U_0)$. The unobservables follow a normal distribution $(U_1, U_0, V) \sim \mathcal{N}(0, \Sigma)$ with mean zero and covariance matrix Σ . Individuals decide to select into treatment if their surplus from doing so is positive $S = Y_1 - Y_0 - C$. Depending on their decision, we either observe Y_1 or Y_0 .

3.2 Model Specification

You can specify the details of the model in an initialization file ([example](#)). This file contains several blocks:

SIMULATION

The *SIMULATION* block contains some basic information about the simulation request.

Key	Value	Interpretation
agents	int	number of individuals
seed	int	seed for the specific simulation
source	str	specified name for the simulation output files

ESTIMATION

The *ESTIMATION* block determines the basic information for the estimation process.

Key	Value	Interpretation
agents	int	number of individuals for the estimation simulation
file	str	specified data inout file for the estimation process
optimizer	str	optimizer used for the estimation process
start	str	determines which start values are used for the estimation process

TREATED

The *TREATED* block specifies the number of covariates determining the potential outcome in the treated state and the values for the coefficients β_1 .

Key	Value	Interpretation
coeff	float	intercept coefficient
coeff	float	coefficient of the first covariate
coeff	float	coefficient of the second covariate
...		

UNTREATED

The *UNTREATED* block specifies the number of covariates determining the potential outcome in the untreated state and the values for the coefficients β_0 . Note that the covariates need to be identical to the *TREATED* block.

Key	Value	Interpretation
coeff	float	intercept coefficient
coeff	float	coefficient of the first covariate
coeff	float	coefficient of the second covariate
...		

COST

The *COST* block specifies the number of covariates determining the cost of treatment and the values for the coefficients γ .

Key	Value	Interpretation
coeff	float	intercept coefficient
coeff	float	coefficient of the first covariate
coeff	float	coefficient of the second covariate
...		

DIST

The *DIST* block specifies the distribution of the unobservables.

Key	Value	Interpretation
coeff	float	σ_{U_0}
coeff	float	σ_{U_1, U_0}
coeff	float	$\sigma_{U_0, V}$
coeff	float	σ_{U_1}
coeff	float	$\sigma_{U_1, V}$
coeff	float	σ_V

SCIPY-BFGS

The *SCIPY-BFGS* block contains the specifications for the *BFGS* minimization algorithm. For more information see: [SciPy documentation](#).

Key	Value	Interpretation
disp	bool	set true to print convergence message
max-iter	int	maximum numbers of iterations the minimization process performs
gtol	float	the value that has to be larger as the gradient norm before successful termination
eps	float	value of step size (if <i>jac</i> is approximated)

SCIPY-POWELL

The *SCIPY-POWELL* block contains the specifications for the *POWELL* minimization algorithm. For more information see: [SciPy documentation](#).

Key	Value	Interpretation
disp	bool	set true to print convergence message
maxiter	int	maximum numbers of iterations the minimization process performs
xtol	float	relative error in solution values <i>xopt</i> that is acceptable for convergence
ftol	float	relative error in fun(<i>xopt</i>) that is acceptable for convergence

3.3 Examples

In the following chapter we explore the basic features of the `grmpy` package. The resources for the tutorial are also available [online](#). So far the package provides the features to simulate a sample from the generalized roy model and to estimate the parameters of interest (given a data set) as specified in your initialization file.

Simulation

First we will take a look on the simulation feature. For simulating a sample from the generalized roy model you use the `simulate` function provided by the package. For simulating a sample of your choice you have to provide the path of your initialization file as an input to the function.

```
import grmpy

grmpy.simulate('tutorial.grmpy.ini')
```

This creates a number of output files that contains information about the resulting simulated sample.

- **data.grmpy.info**, basic information about the simulated sample
- **data.grmpy.txt**, simulated sample in a simple text file
- **data.grmpy.pkl**, simulated sample as a pandas data frame

Estimation

The other feature of the package is the estimation of the parameters of interest. The specification regarding start values and the optimizer options are determined in the *ESTIMATION* section of the initialization file.

```
grmpy.estimate('tutorial.grmpy.ini')
```

As in the simulation process this creates a number of output files that contains information about the estimation results.

- **est.grmpy.info**, basic information of the estimation process
- **descriptives.grmpy.txt**, distributional characteristics of the input sample and the samples simulated from the start and result values of the estimation process

CHAPTER 4

Reliability

We document the results of two straightforward Monte Carlo exercises to illustrate the reliability of the `grmpy` package.

We now briefly discuss our software engineering practices that help us to ensure the transparency, reliability, scalability, and extensibility of the `grmpy` package. Please visit us at the [Software Engineering for Economists Initiative](#) for an accessible introduction on how to integrate these practices in your own research.

5.1 Test Battery

We use `pytest` as our test runner. We broadly group our tests in three categories:

- **property-based testing**

We create random model parameterizations and estimation requests and test for a valid return of the program.

- **reliability testing**

We conduct numerous Monte Carlo exercises to ensure that we can recover the true underlying parameterization with an estimation. Also by varying the tuning parameters of the estimation (e.g. random draws for integration) and the optimizers, we learn about their effect on estimation performance.

- **regression testing**

We provide a regression test. For this purpose we generated random model parameterizations, simulated the corresponding outputs, summed them up and saved

both, the parameters and the sums in a json file. The json file is part of the package. Through this the provided test is able to draw parameterizations randomly from the json file. In the next step the test simulates the output variables and compares the sum of the simulated output with the associated json file information. This ensures that the package work accurate even after an update to a new version.

5.2 Documentation

The documentation is created using [Sphinx](#) and hosted on [Read the Docs](#).

5.3 Code Review

We use several automatic code review tools to help us improve the readability and maintainability of our code base. For example, we work with [Codacy](#). However, we also conduct regular peer code-reviews using [Reviewable](#).

5.4 Continuous Integration Workflow

We set up a continuous integration workflow around our [GitHub Organization](#). We use the continuous integration services provided by [Travis CI](#). [tox](#) ensures that the package installs correctly with different Python versions.

CHAPTER 6

Contributing

Great, you are interesting in contributing to the package.

To get acquainted with the code base, you can check out our [issue tracker](#) for some immediate and clearly defined tasks. For more involved contributions, please see our roadmap below. All submissions are required to follow this project-agnostic [contribution guide](#)

6.1 Roadmap

We aim for improvements to the `grmpy` package in three domains: Objects of Interest, Estimation Methods, and Numerical Methods.

6.1.1 Objects of Interest

- adding marginal surplus and marginal cost parameters as presented in Eisenhauer et al. (2015 [\[6\]](#))

6.1.2 Estimation Methods

- implementing polynomial and local-instrumental variable estimation as outlined Heckman et al. (2006 [\[15\]](#))

6.1.3 Numerical Methods

- exploring alternative optimization algorithms to address large estimation tasks

CHAPTER 7

Contact and Credits

If you have any questions or comments, please do not hesitate to contact us directly.

7.1 Development Lead

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7.2 Contributors

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7.3 Acknowledgments

We appreciate the financial support of the [AXA Research Fund](#) and the [University of Bonn](#). We are indebted to the open source community as we build on top of numerous open source tools such as the [SciPy Stack](#) and [statsmodels](#).

CHAPTER 8

Changes

This is a record of all past `grmpy` releases and what went into them in reverse chronological order. We follow [semantic versioning](#) and all releases are available on [PyPI](#).

8.1 1.0.0 - 2018-XX-XX

This is the initial release of the `grmpy` package.

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