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Wealth Inequality, Portfolio choice, and College Education

My research studies the causes and implications of differences in household wealth, income, and consumption using quantitative general equilibrium settings that are consistent with household-level data. I explore frictions that are necessary to reconcile differences in household behavior, over age, income and wealth, with micro data. Moreover, within these environments, I evaluate the aggregate implications of differences across households for the long-run and recessions.

My job market paper, "Inequality, Portfolio Choice, and the Great Recession", studies the impact of differences in households' choice of portfolio on their consumption and how this channel amplifies the Great Recession in an incomplete-markets dynamic stochastic general equilibrium overlapping-generations model with low-yield liquid and high-yield illiquid wealth. Looking at the 2007-2009 SCF panel data, I find that changes in households' portfolios of low-yield liquid assets and high yield illiquid assets varied with their pre-recession wealth and age. My economy with a nontrivial portfolio choice implies more volatile aggregate quantities. Specifically, it predicts a larger drop in aggregate consumption, as seen in the Great Recession, relative to a single-asset economy. In the model, wealthy and older households experience a relatively large fall in their consumption. This is partly explained by their unwillingness to incur transaction costs required to cash in illiquid wealth; as in the micro-data, many do not rebalance their asset portfolios over the recession. In contrast, as asset prices fall, less wealthy, and younger, households re-balance their portfolios by increasing their shares of illiquid wealth. The rise in the savings of these households leads to further decreases in aggregate consumption.

My second paper, "Skill Premia, Wage Risk, and the Distribution of Wealth", challenges the conventional assumption of i.i.d wage shocks in a standard heterogeneous household economy with uninsurable idiosyncratic risk and studies the implications of unobserved heterogeneity, both in the mean and variance of wage processes, on aggregate wealth and income inequality and life-cycle profiles of earnings, income, and wealth by education groups. I document strong evidence of conditional means and variances of wage processes that rise with skills from the PSID using minimum distance estimation. The implications of these estimated skill-specific wage processes are studied in an incomplete-markets quantitative general equilibrium OLG model wherein households choose their education level. A discrete skill choice partly endogenizes earnings risk across households and introduces a channel through which households' schooling decision affect their earnings as well as wealth. I show that, in contrast to a model with a common wage shock, the model with empirically consistent wage processes that differ by skills successfully explains much of aggregate inequality as well as the life-cycle earnings, income, and wealth of skilled and unskilled households. Furthermore, I find that college education subsidies directed at the poor decrease wealth inequality. However, these subsidies reduce the quality of college graduates and increase the quality of those left behind.

My third paper, co-authored with Aubhik Khan, titled "Segmented Asset Market and the Distribution of Wealth", studies the effects of segmented asset markets on wealth distribution in a quantitative OLG model. Using the 2004 SCF data, we find significant heterogeneity in household portfolio choice across ages and wealth levels. First, 30 percent of U.S. households hold high-yield assets defined as stocks, bonds, and mutual and hedge funds. Second, the probability of a household participating in high-yield asset markets increases with age and wealth level. Lastly, wealthy households tend to hold more of their financial assets as high-yield assets. Solving for stationary equilibrium, we find that asset market segmentation is an important source of wealth inequality. Segmented asset markets lead to a substantial increase in wealth dispersion across households. Specifically, an alternative model without market segmentation generates a Gini coefficient for wealth that is approximately 7 to 10 percent lower. Second, we reproduce the empirical findings that households are more likely to hold high-yield assets if they are older and wealthier.