

# Discussion – Wealth, Race, and Consumption Smoothing of Typical Income Shocks

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PAPER BY: PETER GANONG, DAMON JONES, PASCAL NOEL, DIANA FARRELL, FIONA GREIG, & CHRIS WHEAT

DISCUSSION BY: ADI ALADANGADY, FEDERAL RESERVE BOARD\*

\*The views expressed here are those of the authors and do not necessarily reflect those of the Board of Governors or the Federal Reserve System.

# A referee report I received...

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## Major Concerns:

- Do we need another MPC paper? There seems to be another MPC paper coming out each day and I am not sure what the marginal impact of each successive paper is. I believe it is well known that the PIH does not hold. Therefore, when looking at a subset of people with modest financial means (low income + almost always children), it is especially unsurprising that the PIH

# I see where they're coming from...



Deaton Paxon  
(1994)

Shea  
(1995)

Souleles  
(1999)

StephensUnaya  
ma (2012)

Stephens  
(2003)

Shapiro  
Slemrod (2001)

Sahm Shapiro  
Slemrod (2009)

Baker Yannelis  
(2017)

Aladangady et  
al (2021)



Blundell, et al  
(2008)

Johnson, et al  
(2006)

Deaton Paxon  
(1994)

Kargar Rajan  
(2020)

Japelli Pistaferri  
(2014)

Kueng  
(2018)

Baker  
(2018)

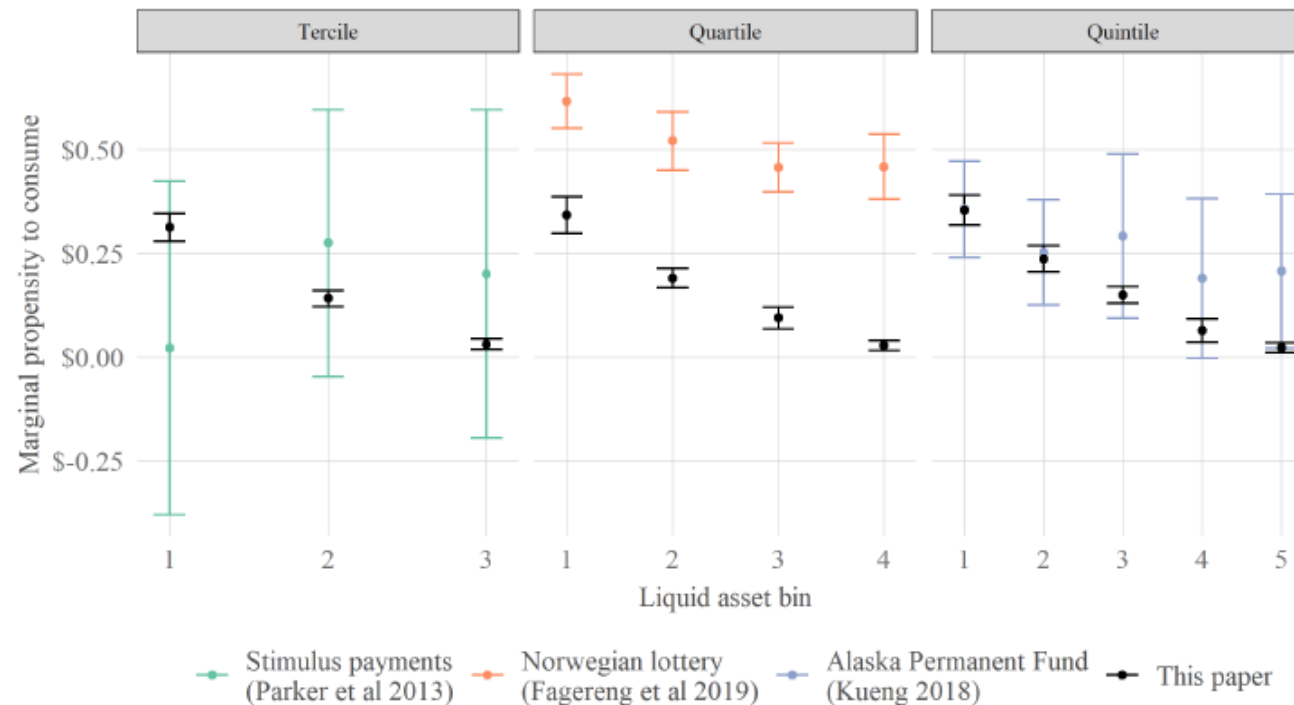
Fagereng et al  
(2018)

Gross et al  
(2020)

# Is this just another one? NO!

Finding 1: Precise estimates of consumption-smoothing provide sharp evidence that MPC's fall with asset holdings

Figure 6: Marginal Propensity to Consume by Asset Buffer

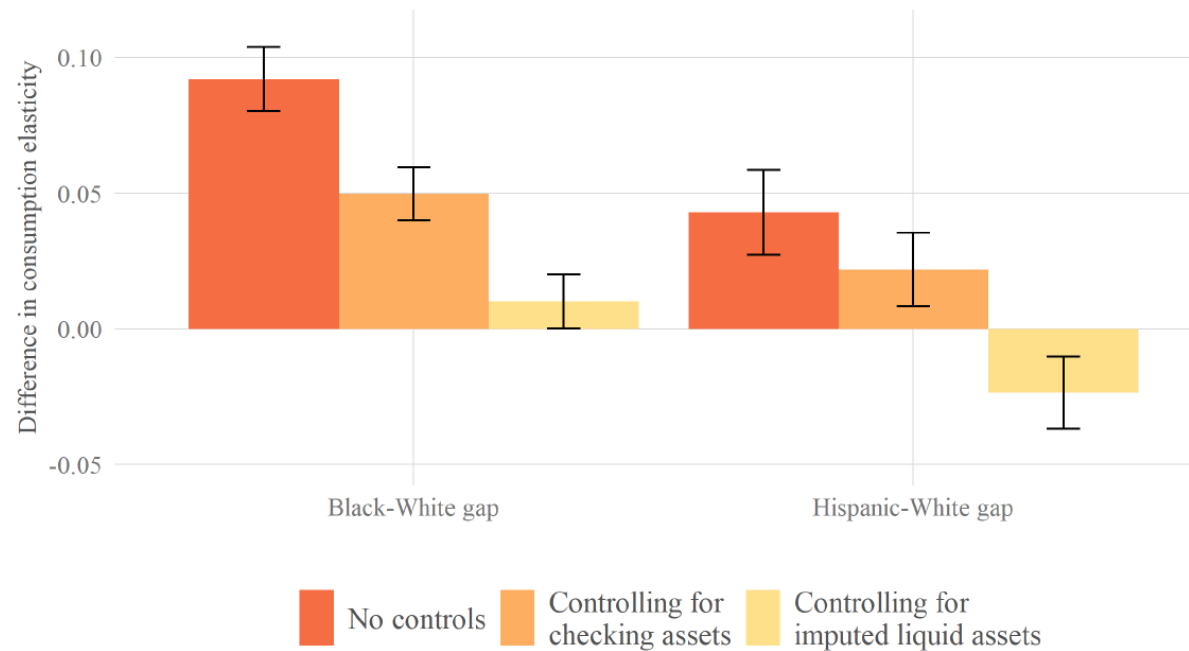


# Is this just another one? NO!

Finding 2: Differences by race, but largely explained by asset holdings.

Figure 7: Racial Inequality in Consumption Smoothing and Role of Assets

(a) Firm Pay Shocks



# Is this just another one? NO!

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Why this matters...

- 1.) Precise estimates of (heterogeneous) MPC's are extremely valuable to policy makers.
- 2.) Policies affecting liquid wealth or credit may reduce consumption volatility.
- 3.) Reducing wealth gaps by race may be sufficient to reduce gaps in self-insurance.

# Comment 1: Information vs Liquidity

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This paper finds MPC's fall with liquid asset holdings

- Nice job handling endogeneity in  $\Delta y$
- Less on endogeneity of liquid buffer (which authors are upfront about)

$$\Delta c = \beta_1 \Delta y * liquidity + \beta_2 \Delta y * [something] + \varepsilon$$

News about earnings and available liquidity on spending interact to generate concurrent covariances between  $\Delta c_t$  and  $\Delta y_t$ .

- Low liquidity –  $\Delta y$  provides cashflow
- Unpredicted –  $\Delta y$  provides information

More unpredictable earnings would...

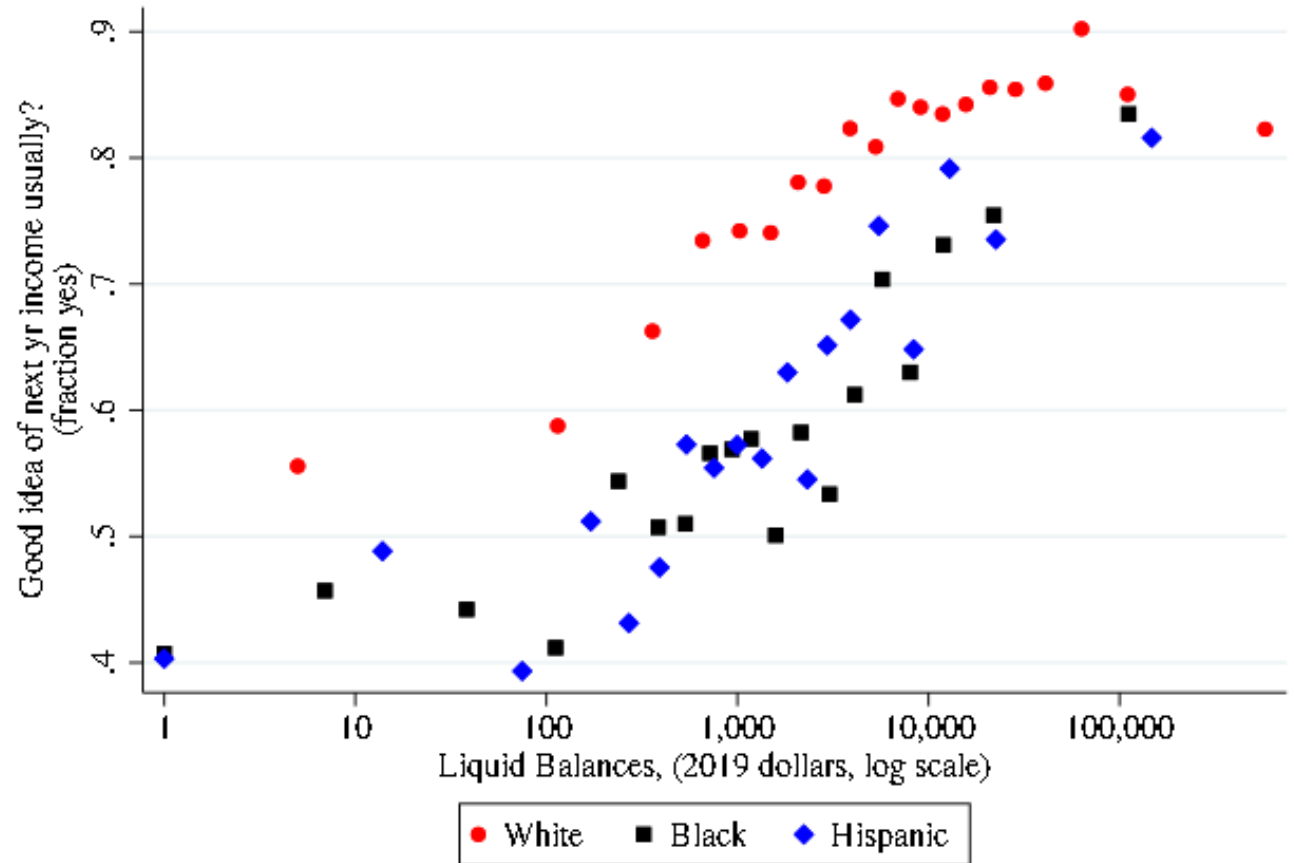
- Make you more sensitive to  $\Delta y \rightarrow$  correlated with MPC
- Leave you with lower balances  $\rightarrow$  correlated with liquid balances

# Comment 1: Information vs Constraints

1. Liquid asset holdings are correlated with forecastability.
2. White workers have more forecastable earnings, even conditional on liquid asset holdings.

Bottom line:

- MPC's by liquidity/race may partly reflect differences in information
- Aligning Black/White wealth may not impact forecastability



Source: Survey of Consumer Finances (2010-2019)



# Comment 2: Identifying Variation/LATE's

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IV excludes labor supply responses (endogenous)

- Does labor supply respond? Is this an insurance mechanism used differently across race/liquidity?

IV captures “synchronous” earnings changes within a firm:

- Bonuses (or annual pay raises)
- Temporary/seasonal fluctuations in hours

IV excludes “asynchronous” earnings changes:

- Job-to-job moves
- Off-cycle pay changes
- Moves to/from unemployment (considered separately)

# Comment 2.1: IV mixes types of variation

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## Why this matters:

- Sources of variation may have different pass-through to spending
- Composition of variation may differ by group.

## High-income worker

- IV picks up bonuses/annual salary changes
- Stable job history and high pay  
→ High (liquid) balances
- More likely white.

## Low-income worker

- IV picks up hours fluctuations
- Unstable job history and low pay  
→ Low (liquid) balances
- More likely minority (Black or Hispanic)

Result – MPC's by race/liquidity may reflect differences in composition of shock!

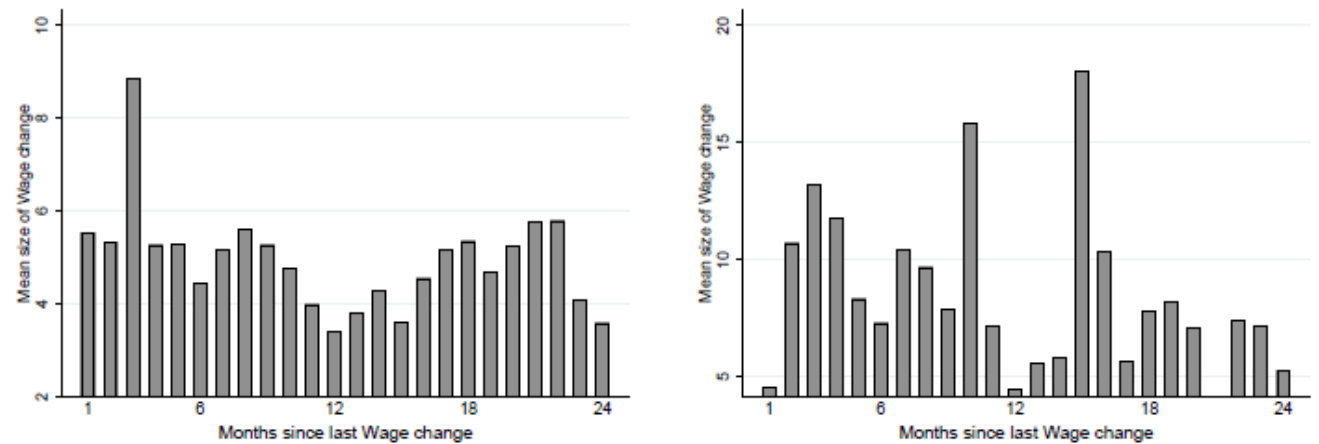
Suggestion: Separate bonuses and hours in data? Other sources of variation?

# Comment 2.2: What the IV leaves out

Asynchronous wage changes are...

- Large compared to synchronous changes (Grigsby, et al 2019)

Figure A9: Mean Size of Base Wage Changes by Time Since Last Change, Job-Stayers



PANEL A: HOURLY WORKERS

PANEL B: SALARIED WORKERS

Note: Figure shows the mean size of base wage increases for workers receiving a base wage increase  $t$  months after their last base wage change. Sample only includes individuals with at least two base wage changes. Additionally, we restrict our analysis to the job-stayer sample.

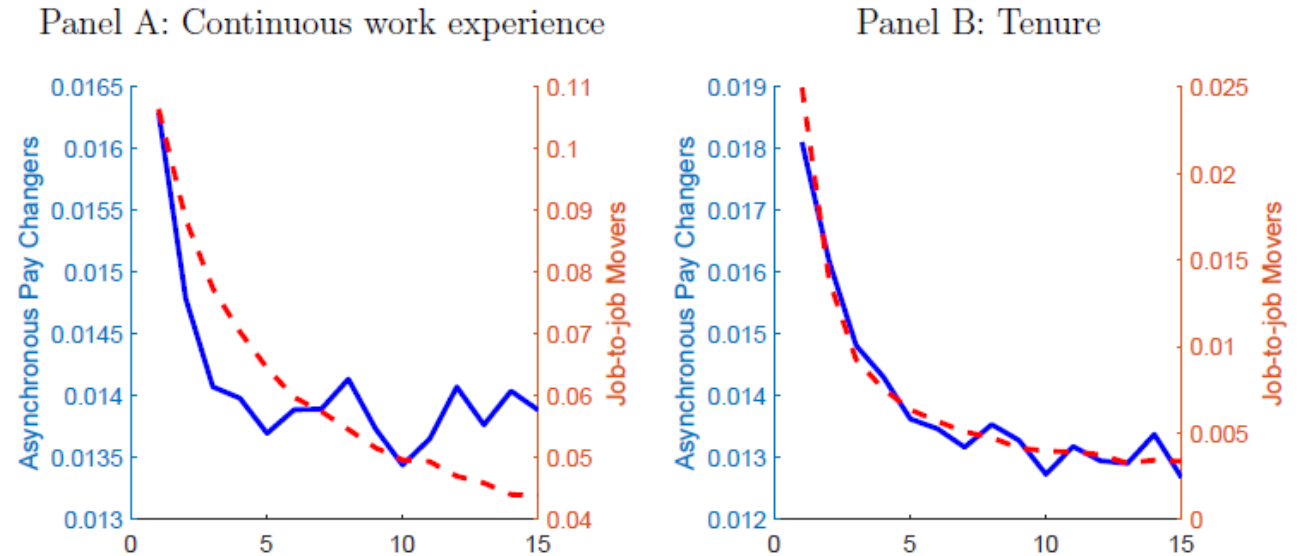
Source: Grigsby, Hurst, Yildamaraz (2019), Figure A9

# Comment 2.2: What the IV leaves out

Asynchronous wage changes are...

- Large compared to synchronous changes (Grigsby, et al 2019)
- Vary with worker tenure (Doniger, 2021)

Figure 2: Incidence of asynchronous pay change declines with seniority



Source: Doniger (2021), Figure 2

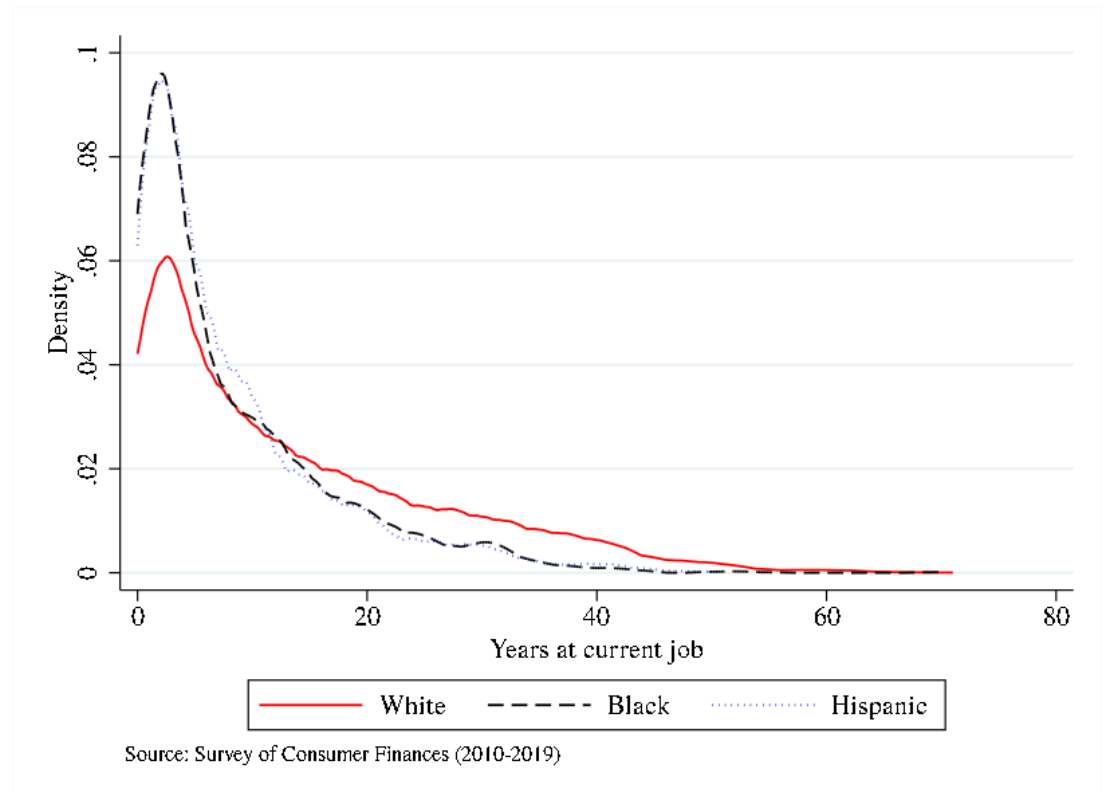
# Comment 2.2: What the IV leaves out

Asynchronous wage changes are...

- Large compared to synchronous changes (Grigsby, et al 2019)
- Vary with worker tenure (Doniger, 2021)

Minority workers have shorter tenures, and more likely to see asynchronous earnings shocks.

Suggestion: Consider consumption volatility in response to these shocks



Source: Survey of Consumer Finances, 2010-2019

# See also

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[Bhutta, Blair, Dettling \(2021\)](#) – Liquid holdings are related to a variety of household factors.

[Doniger \(2021\)](#) – Off-cycle/Asynchronous wage changes are large and have different distribution than on-cycle/synchronous ones

[Murray \(2020\)](#) – Wage changes occur at annual frequency and are synchronized within firm.