Discussion: Unemployment Risk and the Distribution of Assets

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Highlights

- **New insurance channel**
  - ▶ Precautionary job search motive
    - Poor unemployed direct their search towards low wage/low risk jobs
  - ▶ Interaction with standard precautionary savings motive
    - DARA preferences (prudence) imply positive assortative matching

- **Implications**
  - ▶ Lower finding rates for wealthy agents (empirically relevant)
  - ▶ Asset distribution affects job market dynamics (inequality matters!)

- **Policy evaluation and welfare**
  - ▶ Unemployment insurance benefits the poor unemployed
  - ▶ Severance pay hurts the poor unemployed

Key elements

1. **Risk aversion** vs. neutrality
   - makes the problem interesting

2. **Directed search** vs. random [Krusell, Mukoyama, & Sahin, 2010]
   - asset holdings affect job finding probability

3. **Endogenous distribution** vs. degenerate [Acemoglu & Shimer, 1999]
   - allows to think about inequality

4. **Endogenous matching** vs. exogenous [Michelacci & Ruffo, 2014]
   - vacancy creation channel

5. **Non-observable wealth** vs. observable [Chaumont & Shi, 2017]
   - empirically relevant case

Plan for discussion

A) Relative importance of each precautionary motive

B) The role of household debt and default

C) Additional precautionary channels to explore

A) Relative importance of each precautionary motive

- **What's the quantitative role of precautionary search?**
  - Workers are able to endogenously choose the risk they face with their search decision
  - Higher risks $\implies$ higher savings rate if prudence is large enough (requires relative prudence $\frac{-cu'''(c)}{u''(c)} > 2$)

- **Quantitative model uses log (relative prudence $= 2$)**
  - Condition U satisfied (PAM) $\implies$ precautionary job search motive ✓
  - But savings rate do not respond to endogenous risk $\implies$ precautionary savings motive is identical across risk-types

- **Suggestions:**
  - ▶ Compare to a frictionless labor benchmark [Aiyagari, 1994]
  - ▶ Comparative statistics for CRRA parameter γ (risk aversion / prudence), shed light on heterogeneous saving rates

B) The role of household debt and default

- **How does household default distort labor market search?**

- **Model shuts down default**
  - borrowing constraint $a' \geq -\bar{a}$, but debts are always repaid

- **Potential channel: Household debt overhang**
  - Levered households, protected by limited liability, do risk-shifting: search for high wage/risk jobs [Donaldson, Piacentino, Thakor, 2016]
  - An increase in household leverage (negative home equity) causes a decrease in labor supply [Bernstein, 2015]
  - If so, agents with negative assets direct their search as the wealthy!

- **Interesting to explore debt/default channel**

C) Additional precautionary channels to explore

- **Endogenous separation**

  - ▶ Channel: Accept lower wages to avoid separation

  - ▶ Implication? Lower labor mobility (especially for poor)

- **On-the-job-search**

  - ▶ Channel: Job-to-job transition, wage ladder

  - ▶ Implication? Higher labor mobility (especially for wealthy)

- **Final question:** Given that exogenous separation rates λ are the same for all agents, but the wealthy have lower finding rates, the unemployment rate is higher for the wealthy!

  - ▶ Is this true in the model? in the data?

Discussion summary

A) **Relative importance of each precautionary motive**

  ▶ Compare to Aiyagari benchmark and look beyond log preferences

B) **The role of household debt and default**

  ▶ Potential risk-shifting for leveraged agents

C) **Additional precautionary channels to explore**

  ▶ Endogenous separation and on-the-job-search