Wealth Inequality in the US: the Role of Heterogeneous Returns

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QUESTIONS

- Why is wealth so concentrated in the United States?
- Is heterogeneity in the return on saving across households an important driver of US wealth inequality?
  - Relative to e.g. heterogeneity in earnings

STRATEGY

- **Empirical analysis**:
  - Household-level data from the Survey of Consumer Finances (SCF)
  - Match to returns on a number of asset classes (needed to compute capital gains)
  - Calculate average return differences across wealth groups
  - Decompose return differences “within” and “across” asset classes

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- **Empirical analysis**:
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  - Decompose return differences "within" and "across" asset classes
- **Structural model**:
  - Incomplete markets & idiosyncratic income risk & idiosyncratic return risk
  - Ex ante differences in asset return process
  - Carefully calibrate to moments in US data
  - Characterize stationary equilibria with and without return heterogeneity
  - Compare top wealth shares to US data in each case

FINDINGS

- In the data, return differences across the wealth distribution are massive
  - Between 20th and 99th percentile, average return moves from 3.6% to 8.3%
  - Driven strongly by portfolio composition, but also within asset classes

- In the model, earnings and return heterogeneity can *fully* explain wealth inequality
  - Without return heterogeneity, top 10% wealth share = 36% (data: 76%)

COMMENTS

1. Data limitations and implications for framing the paper
2. Savings shares along the wealth distribution
3. Thinking about general equilibrium forces

COMMENT 1: DATA LIMITATIONS & FRAMING

Several disadvantages of SCF data ...

1. Not a true panel, income/wealth is self-reported, etc.
   - In fact, a lot of the competition in this literature uses administrative data
2. Within asset class heterogeneity only comes from income flow component
   - Capital gains variation is computed by asset type and not by individual saver

COMMENT 1: DATA LIMITATIONS & FRAMING

- On 1., perhaps emphasize more the US focus?
  - More emphasis along the lines of "... differs in several ways from Scandinavian economies, including in the degree of wealth inequality"
- On 2., make clearer that this might underestimate the true return heterogeneity within asset classes?

COMMENT 2: SAVINGS SHARES ALONG THE WEALTH DISTRIBUTION

- With CRRA preferences (and without labor supply decisions, bequest motives, ...) savings shares should be linear in wealth
- I suspect that due to the ex ante differences in returns, higher return types have higher savings rates
- So high return types collect better returns, but also *save larger quantities*
    - Unpacking this effect could make the model even more interesting

Comment 2: Savings shares along the wealth distribution

- Savings shares that increase with income are actually empirically plausible
- Calculating savings shares as a function of income in the model could provide another untargeted moment to evaluate the model
- Furthermore, it might be possible to decompose how much wealth inequality comes from the “price effects” and “quantity effects” of return heterogeneity

COMMENT 3: THINKING ABOUT GENERAL EQUILIBRIUM FORCES

- In the model, returns are exogenous
- If returns adjusted in general equilibrium, it could be that more wealth inequality could drive down the returns of higher return assets
- Whether this economic force is important in practice is an interesting question
  - Food for thought, probably for a separate paper

CONCLUSION

- Great contribution to an important area of research
- Very competent combination of data and quantitative model
- Gives inspiration for future work