Consumption Smoothing and Intertemporal Substitution versus the Household Financial Squeeze in the Great Recession

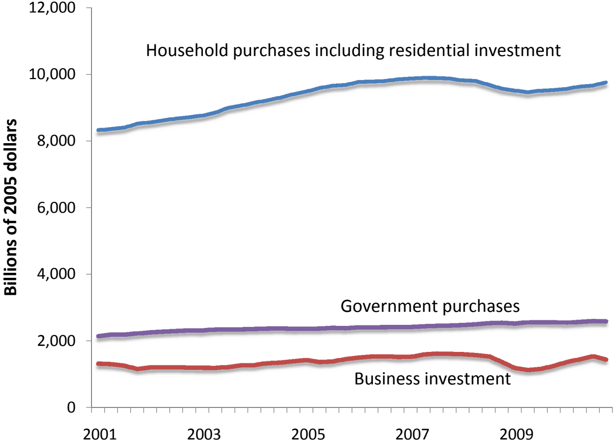
Robert E. Hall
Hoover Institution and Department of Economics
Stanford University

JRC Third Annual Conference
Princeton University

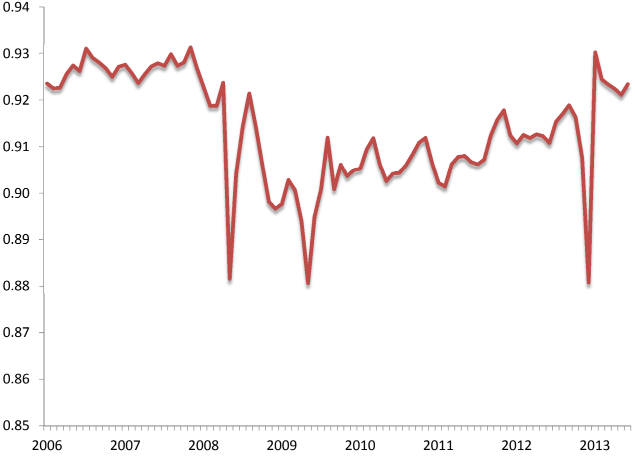
February 20, 2014

.

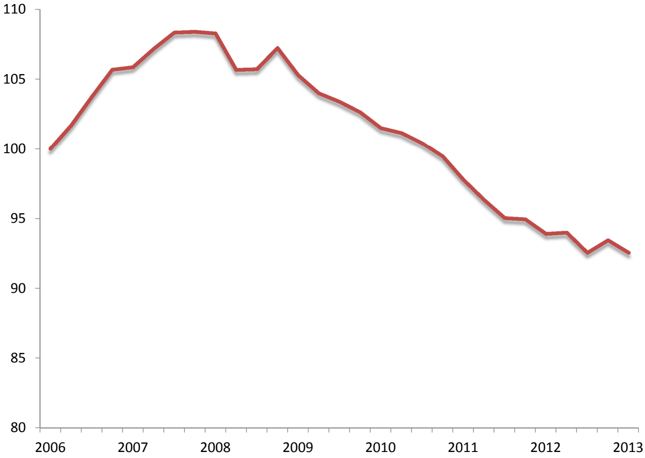
Household purchases dominated the movements of GDP in the Great Recession



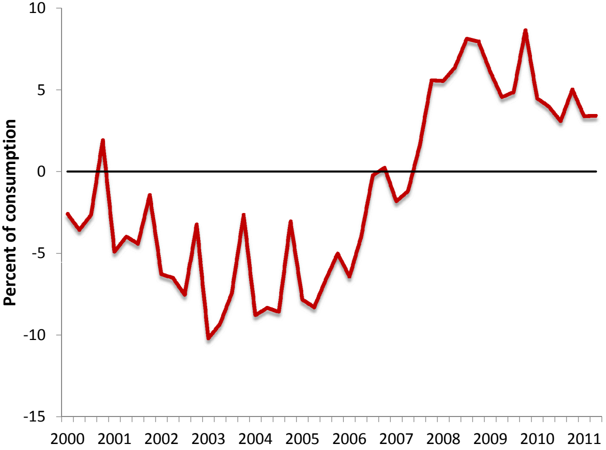
The Ratio of Consumption to Disposable Income



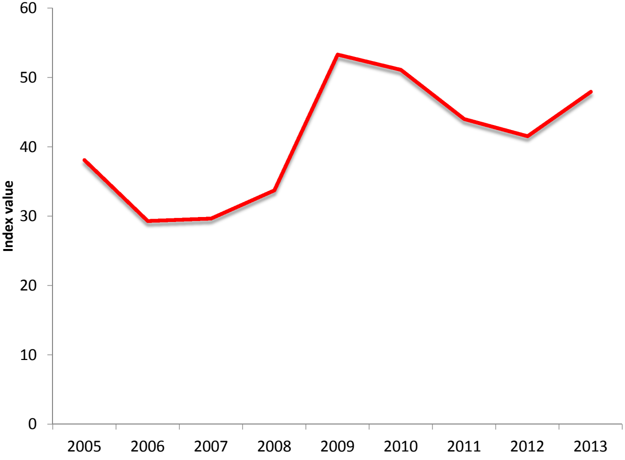
Real Household Liabilities



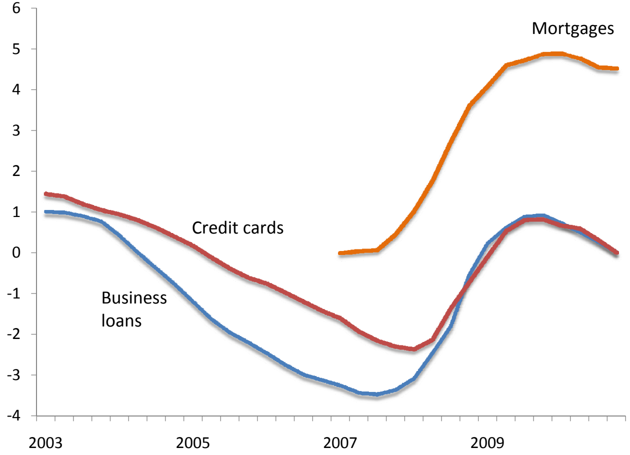
Burden of Deleveraging as a Percent of Consumption



Google searches for "withdrawal penalty"



Indexes of Lending Standards Inferred from the FRB Senior Loan Officer Survey



Intertemporal substitution

$$\Delta \log c_t = \sigma(d_t - \rho)$$

Intertemporal substitution

$$\Delta \log c_t = \sigma(d_t - \rho)$$

d_t is the consumption-relevant discount rate and ρ is the rate of impatience

Intertemporal substitution

$$\Delta \log c_t = \sigma(d_t - \rho)$$

d_t is the consumption-relevant discount rate and ρ is the rate of impatience

d_t captures the financial risk (correlation with marginal utility) of future consumption

Intertemporal substitution

$$\Delta \log c_t = \sigma(d_t - \rho)$$

d_t is the consumption-relevant discount rate and ρ is the rate of impatience

d_t captures the financial risk (correlation with marginal utility) of future consumption

Increase in d_t alters consumption plans toward higher growth, and thus lower current consumption

.

Discount Rate for the S&P Stock-Price Index