



# Household heterogeneity in the euro area since the onset of the Great Recession<sup>☆</sup>

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Received 12 April 2015; received in revised form 23 July 2015; accepted 5 September 2015  
Available online 25 September 2015

## Abstract

We propose a simple and transparent tool to extend household-level data from the Household Finance and Consumption Survey using aggregate series and micro-simulations. We quantify shocks to wealth and financial pressure faced by various categories of households since the onset of the Great Recession. The shocks differ substantially across countries and across economic and socio-demographic characteristics. We find that the rising unemployment rate disproportionately affected the income-poor, while the declining asset prices more the income-rich. Although borrowers benefited from lower interest rates, debt service-income and debt-income ratios for poor households went up due to falling incomes. As a policy contribution we illustrate how our “pseudomicro data” can be used to assess the distributional impact of asset prices on consumption: the unprecedented declines in asset prices substantially contributed to the sluggish consumption growth driven by both rich and poor households. While the former were hit by large shocks to wealth, the latter also significantly cut their spending because of their high MPCs.

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<sup>☆</sup> This paper uses data from the Eurosystem Household Finance and Consumption Survey. We thank John Sabelhaus, anonymous referees, the editor, and seminar participants at the ECB and the Eurosystem Household Finance and Consumption Network for useful comments. The views presented in this paper are those of the authors, and do not necessarily reflect those of the European Central Bank or the Deutsche Bundesbank. For an extended version of this paper, see [Ampudia, Pavlickova, Slacalek, and Vogel \(2014\)](#).

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*JEL classification:* D12; D31; E21

*Keywords:* Household heterogeneity; Financial pressure; Wealth effect; Great Recession; Household Finance and Consumption Survey

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## 1. Introduction

During the Great Recession, economic activity in the euro area declined by 6 percent in real terms and has not recovered for more than five years thereafter. Most households faced a prolonged series of considerable adverse shocks to their income and a decline in their housing wealth unprecedented in the post-war era.

The aggregate figures hide considerable heterogeneity at the micro level—for households with various social, demographic and economic characteristics living in different countries—pervasive for many economic variables, including holdings of various assets. The dynamics of asset prices were diverse, both across countries and across asset classes. Given the substantial differences in participation rates and holdings of various assets, changes in prices of various assets affected the distribution of wealth across households.

This paper develops a method to approximate the evolution of the distribution of income, wealth and debt service by combining household-level data from the Eurosystem Household Finance and Consumption Survey (HFCS) with country-level aggregate time series (Section 2). The HFCS covers in detail balance sheets, income and indicators of consumption of more than 62,000 households from fifteen euro area countries, giving a comprehensive snapshot of household heterogeneity during its reference year, mostly 2010. We complement this cross-sectional information with the dynamics captured in aggregate macroeconomic and financial data, and provide a timely approximation of household heterogeneity, a method we call “mechanical extension” below. In addition, we use micro-simulation models to account for the recent substantial increase in the unemployment rate (across many countries), a method we call “unemployment simulation” below.

The main contribution of the paper is to construct a transparent tool to approximate “intermediate releases” of micro data described in a timely manner and to undertake simple, rule-of-thumb calculations (such as the one on the effects of wealth on consumption). We first document shocks to wealth and debt service experienced by various categories of households (Section 3). While much of the variation stems from cross-country developments, important differences among households exist even within countries, because holdings of various classes of assets and liabilities, and unemployment rates vary substantially over economic and socio-demographic characteristics. For example, we find that the increase in the unemployment rate has disproportionately affected income-poor households, while the decline in asset prices the income-rich. Although borrowers benefited from the substantial decline in interest rates, debt service-income and debt-income ratios for poor households rose because of the drop in their incomes.

As an additional policy contribution we then illustrate how our “pseudomicro data” can be used to assess the distributional impact of asset prices on consumption (Section 4). Because empirical evidence strongly suggests that spending of poor households reacts more to shocks, we allow for variation in the marginal propensity to consume (MPC) across the income distribution. Under such scenario, the drop in spending is caused by both rich and poor households: while the former

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