



HANK BY KMV

COMMENTS BY ERM

JUNE 2017



## What They Do

- Compare impact of monetary shock for RANK & HANK
  - Total initial responses of consumption
  - And a decomposition:
    - Direct effect:* Hold labor income fixed
    - Indirect effect:* Allow changes in labor income
- Claim: need this for “successful conduct” of policy



## Contribution

- Now, lots of analyses of monetary transmission in HANK
- But, analyze rich model of consumption/savings behavior



## What They Find

	$d \log C / dr$	% Direct Effect
RANK-SW	-0.7	99
RANK-KMV	-2.1	94
HANK-KMV	$[-1.7, -2.9]$	$[19, 42]$

SW = Smets-Wouters estimate for estimated model of US



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RANK-KMV elasticity 3 times larger



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HANK elasticity not necessarily larger, depends on fiscal policy



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KMV emphasize direct effect



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Which is large if there are few “hand to mouth” households





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And small if there are many “hand to mouth” households



## Potential Audiences

- Business cycle analysts
- Monetary policy analysts
- Fiscal policy analysts

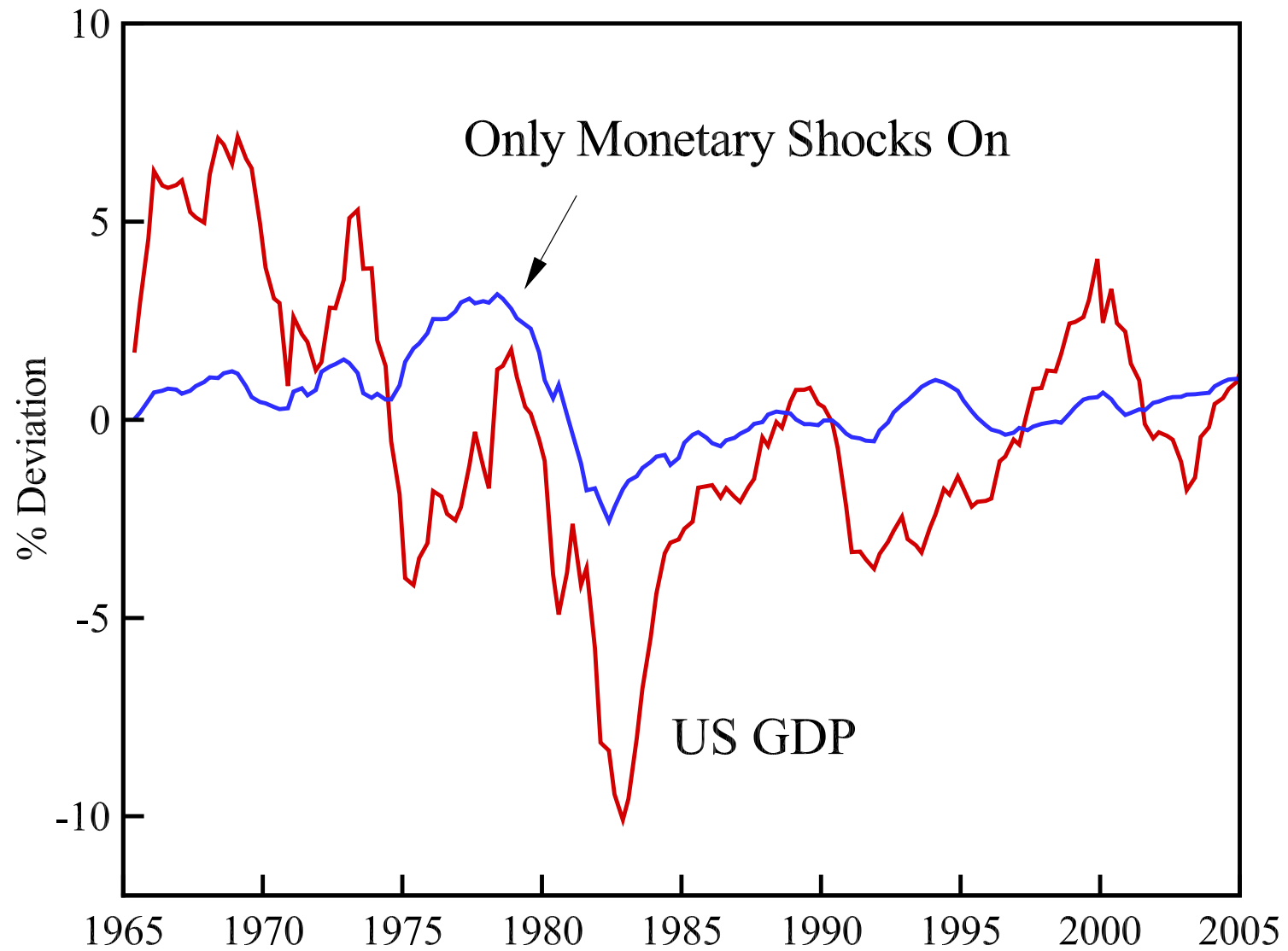


## Business Cycle Analysts

- Should they give up RANK?
- No, differences in aggregate predictions too small



# Predictable from SW Results



GDP, US Data and Contribution of Monetary Shocks



## Monetary Policy Analysts

- Should they give up RANK?
- Possibly, but KMV need to show
  - If DGP is HANK, RANK users will be unsuccessful
    - HANK with many HtMs is useful abstraction



## RANK Unsuccessful?

- Trade-offs RANK might miss
  - Size versus persistence of shock
  - Inflation versus output

But, results surprisingly similar and hard to detect!



## Is HANK-KMV a Useful Abstraction?

- Key assumptions:
  - Scarce liquidity
  - High transaction costs
  - Fed Funds is relevant interest rate

How realistic?



## Scarce Liquidity? No

	KMV	BOG
Net Worth	3.47	4.56
Liabilities	.80	.90
Real estate	1.71	1.71
Business	.59	.59
Durables	.33	.34
LI & Pensions	—	1.11
Deposits	.47	.48
Bonds	.13	.40
Stocks	1.03	.80
Liquid assets?	.26	1.68





## Scarce Liquidity? No

- And more liquidity from borrowing against:
  - Home equity
  - Business equity
  - Life insurance and pension assets



## High Transaction Costs? No

- Exchange-traded funds (ETF)
  - No fees
  - 1 share minimum



# Why are Households on Corners?



## Why are Households on Corners?

- One major reason is college financial aid
  - 70% of full-time students receive aid
  - 46% of student budget covered
- House, pensions, business not counted on FAFSA

⇒ Optimal to look *as if* hand to mouth



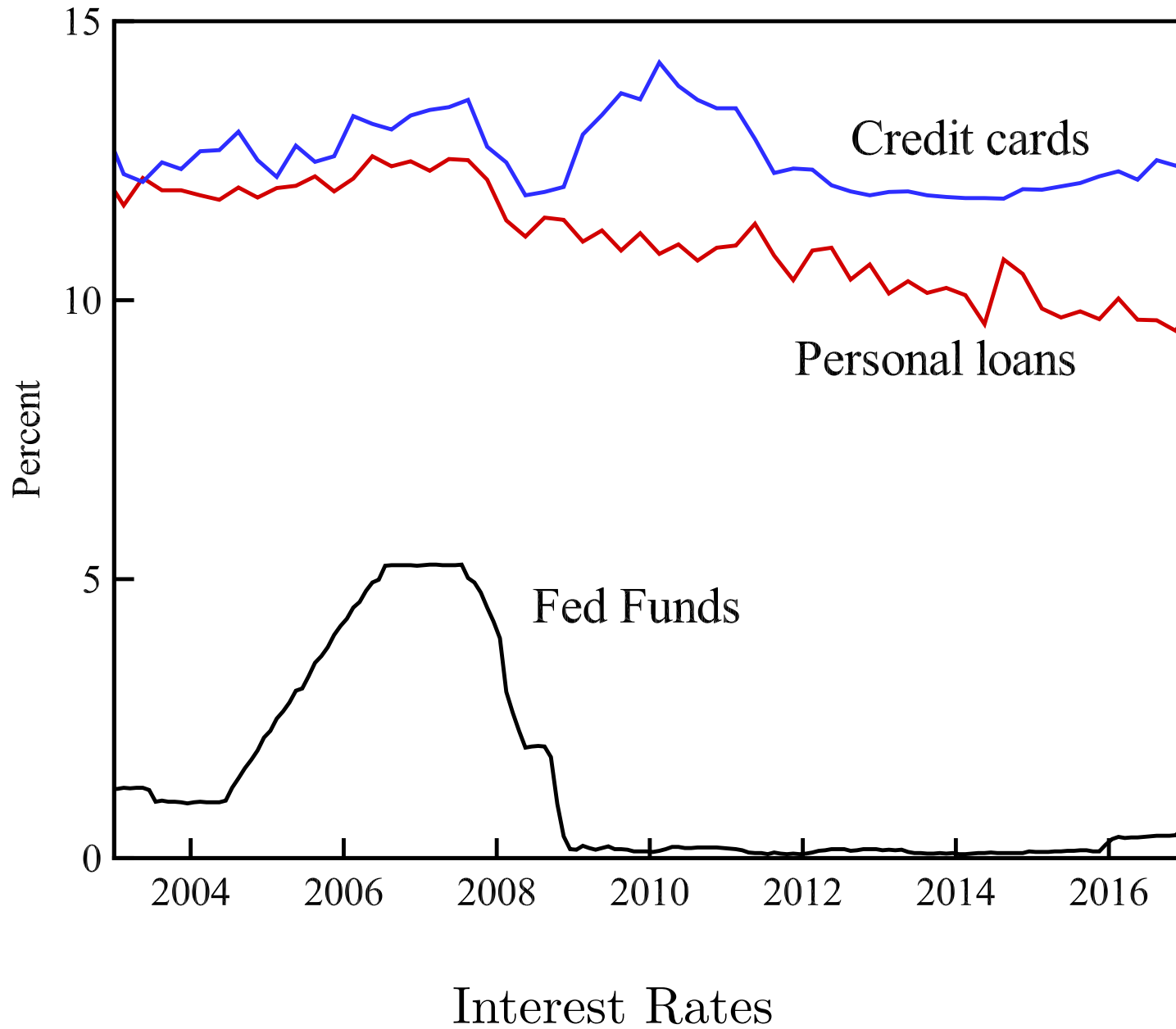
## Fed Funds Rate Relevant? Not likely

- Relevant rates:
  - Credit cards
  - Personal loans

which barely move in response to Fed actions



# Fed Funds Rate Relevant? Not likely





# Fiscal Policy Analysts

- Quantitative results depend on fiscal policy
- Specifically, how is budget balanced?
  - Transfers?
  - Debt?
  - Distortionary taxes?



## Fiscal Policy Analysts

- Should they give up RANK?
- Possibly in favor of RA or, better yet, HA





## Fiscal Policy Analysts

- Should they give up RANK?
- Possibly in favor of RA or, better yet, HA
- KMV could consider new title:

*Fiscal Policy According to HA*



## Main Recommendations

- If stick with HANK ...
- Show
  - If DGP is HANK, RANK users will be unsuccessful
  - HANK with many HtMs is useful abstraction
- Clarify
  - What successful conduct of monetary policy means
  - Why knowing direct/indirect split is essential