DISCUSSION ON

"TIME-VARYING WAGE RISK, INCOMPLETE MARKETS, AND BUSINESS CYCLES"

BY SHUHEI TAKAHASHI

Ahmet Ali Taskin

Question?

- How much cyclical variation in idiosyncratic earnings risk affects labor market dynamics?
  - Fluctuations in labor wedge
  - Correlation between total hours worked and average labor productivity

Model

- Heterogenous-agent incomplete assets markets model with time-varying idiosyncratic wage risk and indivisible labor
  - Except for the time-varying wage risk it is standard both for modeling and calibration
- Calibrate uncertainty shocks and idiosyncratic productivity to individual wage data in the PSID.
  - Contribution of the paper

MODEL

- Perform an OLS estimation with dynamic controls on individual wage observations
- Estimate persistence of the idiosyncratic productivity (observed wage)
- Obtain dispersion using residuals (wage risk)
  - Why does the procedure differ between section 2 and 4?
- Obtain average dispersion over time, persistence and volatility of the dispersion
  - Very critical

MAİN EXERCİSE/RESULTS

- Temporary increase in the idiosyncratic wage risk
  - Output increases slightly, then returns to original levels
  - Hours first increases, then decreases below pre-shock level, later slowly reverts to the mean
  - Labor productivity moves in the opposite direction
  - Hence, negative co-movement of hours with productivity
- First period: uncertainty effect
  - Higher uncertainty induces an increase in labor supply for everyone
  - Would that increase with more risk averse individuals?

Main exercise/results

- Second period: distribution effect
  - Increase in productivity dispersion
  - More low (high) productivity – low (high) wealth individuals
  - Decrease (increase) in labor supply for low (high) productivity individuals
  - Low productivity individuals dominate the outcome
  - The recovery is slow due to high persistence in productivity
- The contribution of the second effect is stronger
  - The psych risk model a la Bachman and Bayer (2013) explains 27% percent of labor wedge volatility and suffers the hours puzzle

REMARKS

- Counter-cyclical wage risk:
  - Guvenen, Ozkan and Song (2014): variance is not cyclical, skewness is cyclical (i.e. during recessions large downward (upward) movements become more (less) possible.)
- Individual labor supply elasticity needs to high for the distribution effect to operate?
- What about joint labor supply decisions?