Essays on frictions and inefficiency in housing and regional labor markets
Lalit Contractor

My dissertation examines the efficiency implications of various frictions (financial, trading or labor market) in housing and regional labor markets.

1 Inefficient mortgage defaults: theory and application to the housing downturn (job market paper)

This paper describes the inefficiencies associated with mortgage defaults in a standard equilibrium housing model. I calibrate the model to the U.S. housing market and evaluate these inefficiencies in a simulated downturn that captures the peak foreclosure spike and house price decline in the Great Recession. I find that the deadweight cost inefficiency associated with realized lender losses from foreclosure dominates pecuniary externalities, which are insignificant. Debt renegotiation mitigates lender losses following default but might be inefficiently low when transaction costs are incurred prior to the renegotiation process.

2 Externalities and inefficiency in an intermediated directed search model of the housing market

This paper derives inefficiencies associated with house sale choices in a frictional model of the housing market. Trading frictions are modeled using a broker-intermediated directed search framework. The inefficiency results arise due to pecuniary externalities and are robust to extensions incorporating frictional house purchases and defaultable debt. A novel finding is that pecuniary externalities also lead to inefficiencies in the market tightness or sale list price choice. For example, if house sellers are more constrained than buyers, then private sellers list prices that are lower than the efficient list price.

3 Sorting, migration and the informal sector (in progress)

This paper develops a model that yields both the observed rural-urban ability driven wage gaps and limited, asymmetric regional migratory flows. It investigates the relative importance of mismatch risk and migration costs in deterring rural-urban migration for higher ability workers (leading to misallocation), and explores when lower ability urban workers would prefer to work in the urban informal sector rather than migrate. From a policy perspective, relaxing regulations limiting the productivity of the urban informal sector might exacerbate the asymmetric migratory flows.