

(19) Alessandri, Piergiorgio. "Aggregate Consumption and the Stock Market: A New Assessment of the Equity Wealth Effect." University of London, 2003.

The author analyzes the short run linkage between stock market and aggregate consumption, in order to assess the claims that consumers react differently to negative and positive changes in their equity wealth, by comparing whether the data displays nonlinearities using non-parametric techniques against the linear econometric models that have been extensively used to analyze this issue. The paper argues that if there are reasons to believe that consumption may adjust nonlinearly to movements in equity prices, semi parametric techniques allow a completely unrestricted analysis of the adjustment process.

The nature of the short run aggregate equity wealth effects are investigated using monthly data, as equity prices fluctuate substantially over short horizons, and thus a good deal of information is lost when looking at changes in longer periods of time that has been usually considered in the literature.

A long run relationship between consumption of non durables, equity wealth and nonequity wealth, finds that the marginal propensity to consume out of equity wealth is much smaller than that out of nonequity wealth, possibly due to higher volatility of equity values and the higher concentration of equity ownership. Short run dynamics are described by a vector error correction model, and show that it is equity wealth that adjusts in the long run. The author also concludes that the stock market is not an important factor in determining individual consumption choices in the short run, and impulse response analyses show that the response of consumption after an equity price shock is not significantly different from zero.

The author conducts a semi parametric investigation of the short run where no functional restriction is placed on the linkage between equity prices and consumption, and concludes that the linear and nonlinear alternatives are virtually indistinguishable, the linear model is never rejected, and the claim that the wealth channel is asymmetric and that consumers are more sensitive to stock market falls is rejected by the data.

The author finally concludes that these results provide further evidence that linearity is a reasonable working assumption, and that consumption decisions are largely independent of stock market fluctuations.