

**(11) Mehra, Yash. "The Wealth Effect in Empirical Life Cycle Aggregate Consumption Equations." Federal Reserve Bank of Richmond Economic Quarterly, 87/2, 2001.**

The paper investigates whether wealth has predictive content for future consumption. The author estimates long run consumption equations that relate consumption to labor income and total wealth, and another where total wealth is decomposed into equity and nonequity components, where the coefficients measure the long run MPC out of income and wealth, in addition to estimating the corresponding short run consumption equations that relate changes in actual consumer spending to changes in income and wealth variables allowing for the presence of lags in the adjustment of actual consumption to planned consumption.

From the long run estimates, labor income and wealth variables have the expected signs and are significant, and indicating that a one dollar increase in wealth raises consumer spending by 3 cents, and that a one dollar increase in equity values raises consumer spending by 3 to 4 cents.

Estimating the short run consumption equations, the author finds that all estimated coefficients appear with theoretically expected signs and are statistically significant, where the negative coefficient on the error correction term indicates the presence of adjustment lags in consumer spending, and others show that spending respond to current period changes in income and wealth. Also, the results reflect that the short term elasticity is smaller with respect to changes in equity values than with respect to changes in total or nonequity wealth.

The paper attempts at quantifying the effect of the stock market boom on consumer spending, and found that equity wealth effect represented an increment to the growth rate of real GDP of about 1 percentage point per year, and that total wealth effect may have added to the growth rate of real GDP about 2 percentage point per year.