

Political Aspects of Household Debt

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Abstract

The recent literature has shown that income inequality is one of the main causes of borrowing and debt accumulation by working households. This paper explores a different dimension. We investigate whether household indebtedness is an important cause for rising income inequality. If workers experience rising debt burden, workers job security and bargaining power for a higher wage can diminishes as they need income to continue debt service payments. This in turn increases income inequality and induces workers to borrow more. We believe this is an important channel why we observed rising income inequality and household debt accumulation simultaneously in the countries that experienced a crisis recently. To explore this channel, we develop an employment rent framework that explicitly considers the impact of workers indebtedness on their cost of job loss. Furthermore, based on this employment rent framework, we develop a neo-Kaleckian macro model to analyze the dynamic relationship between household debt and income inequality.

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