Consumption Smoothing without Secondary Markets for Small Durable Goods*

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Abstract

The purpose of this paper is to study whether trade frictions in durable goods markets help account for the patterns of household consumption expenditures observed in the *Consumer Expenditure Survey* (CEX), namely that the response of durable goods expenditures to income shocks is 78 percent larger than that of nondurable goods and the variance of the idiosyncratic part of log durable goods expenditures is four times as high as that of log nondurable goods expenditures. To do so, I develop a model with a continuum of households who purchase durable as well as nondurable goods. The key assumption is that durable goods cannot be rented or sold after purchase. By comparing stationary distributions of the model with and without trade frictions, I find that trade frictions are crucial to account for the expenditure patterns observed in the data.

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