Masked financial instability caused by wealth inequality

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We investigate masked financial instability caused by wealth inequality. When an economic sector is decomposed into two subsectors that possess a severe wealth inequality, the sector in entirety can look financially stable while the two subsectors possess extreme financially instabilities of opposite nature, one from excessive equity, the other from lack thereof. The unstable subsector can result in further financial distress and even trigger a financial crisis. The market instability indicator, an early warning system derived from dynamical systems applied to agent-based models, is used to analyze the subsectoral financial instabilities. Detailed mathematical analysis is provided to explain what financial instabilities can arise amid seemingly stable economy and positive market data. The theoretical conjecture is verified by historical macroeconomic time series of the United States households among whom a substantial wealth inequality has been officially confirmed.

References

[1] Choi, Y. , *Masked Instability: Within-Sector Financial Risk in the Presence of Wealth Inequality* , Risks 2018, 6(3), 65