

When Preferences Cap Consumption: A Scrooge McDuck Theory of Wealth Dynamics

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Abstract :

This paper presents a new theoretical mechanism that accounts for the joint evolution of the wealth-to-output ratio, wealth inequality and investment observed over recent decades in advanced economies. Agents derive utility from holding wealth and their preferences define an upper-bound on optimal consumption. After a certain period, some agents, labeled as Scrooge McDuck, consistently receive earnings above this consumption cap and increase their asset holdings in every period. This persistent asset demand supports the existence of rational bubbles, which crowd out investment. The rate of return on these bubbles exceeds the growth rate of the economy, and the bubble-to-output ratio is diverging. The aggregate bubble size is uniquely defined such that non-Scrooge McDuck agents hold no bubble units asymptotically. Wealth inequality is positively correlated with bubble price and diverging.