Income Volatility and Portfolio Choices*

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Abstract

Based on administrative data from Statistics Norway, we find economically significant shifts in households' financial portfolios around individual structural breaks in labor-income volatility. According to our estimates, when income risk doubles, households reduce their risky share of financial assets by 5 percentage points, thus tempering their overall risk exposure. We show that our estimated risky share response is consistent with a standard portfolio choice model augmented with idiosyncratic, time-varying income volatility.

JEL Classification: E2, G1, J3.
Keywords: Income Volatility, Portfolio Choice, Risky Share

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