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# **Stabilising and destabilising factors of 14 EU housing markets**

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## Research Focus and Questions

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- Intention: to cast some light on a more broader set of factors which impacted on the recent housing market cycles in Europe, including factors beyond macroeconomic fundamentals
- Questions:
  - How did the core variables of house prices and housing investment develop in 14 EU-countries between 1995 and 2011? What stands out compared to former housing market cycles?
  - Which were important common factors, which were important country-specific factors?
  - Which factors made for differences, which for parallelism in developments?

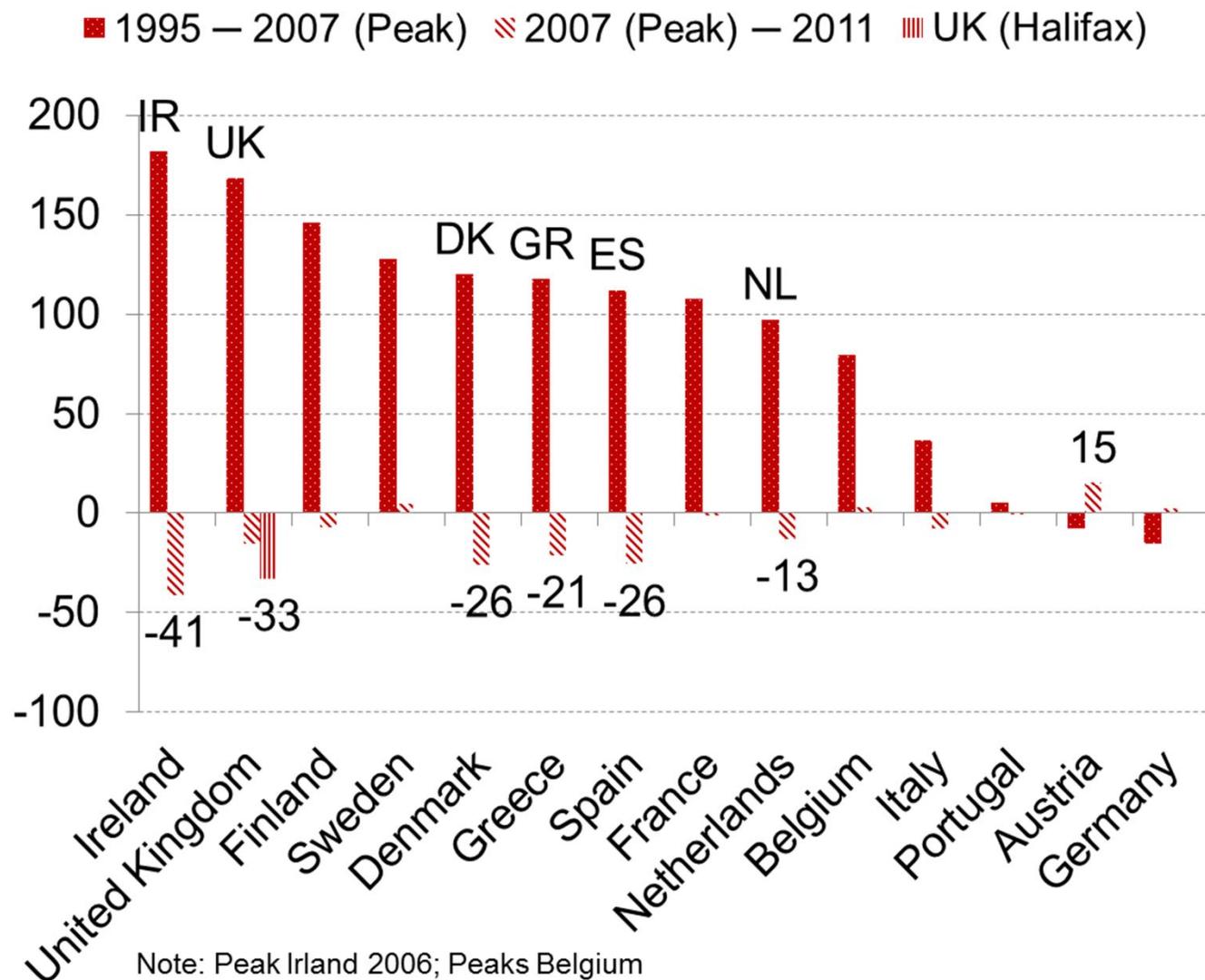
A Note: As all of the booming housing markets had their house price peaks in or around 2007, this year acts a natural divide in two research periods

- pre-crisis: 1995–2007
- downswing: 2007–2011–??

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# The recent housing market cycle(s) in the EU-14

# Real House Prices Change (in %)



A broad trend of soaring house prices betw. 1995 and 2007:

- 10 markets booming
- Real HP more than doubled in 8 markets
- Bust in 5 markets after 2007

4 countries were bucking the trend

⇒ A classification acc. to HP-developments:

Boom – Bust :

IR, UK, DK, GR, ES, (NL)

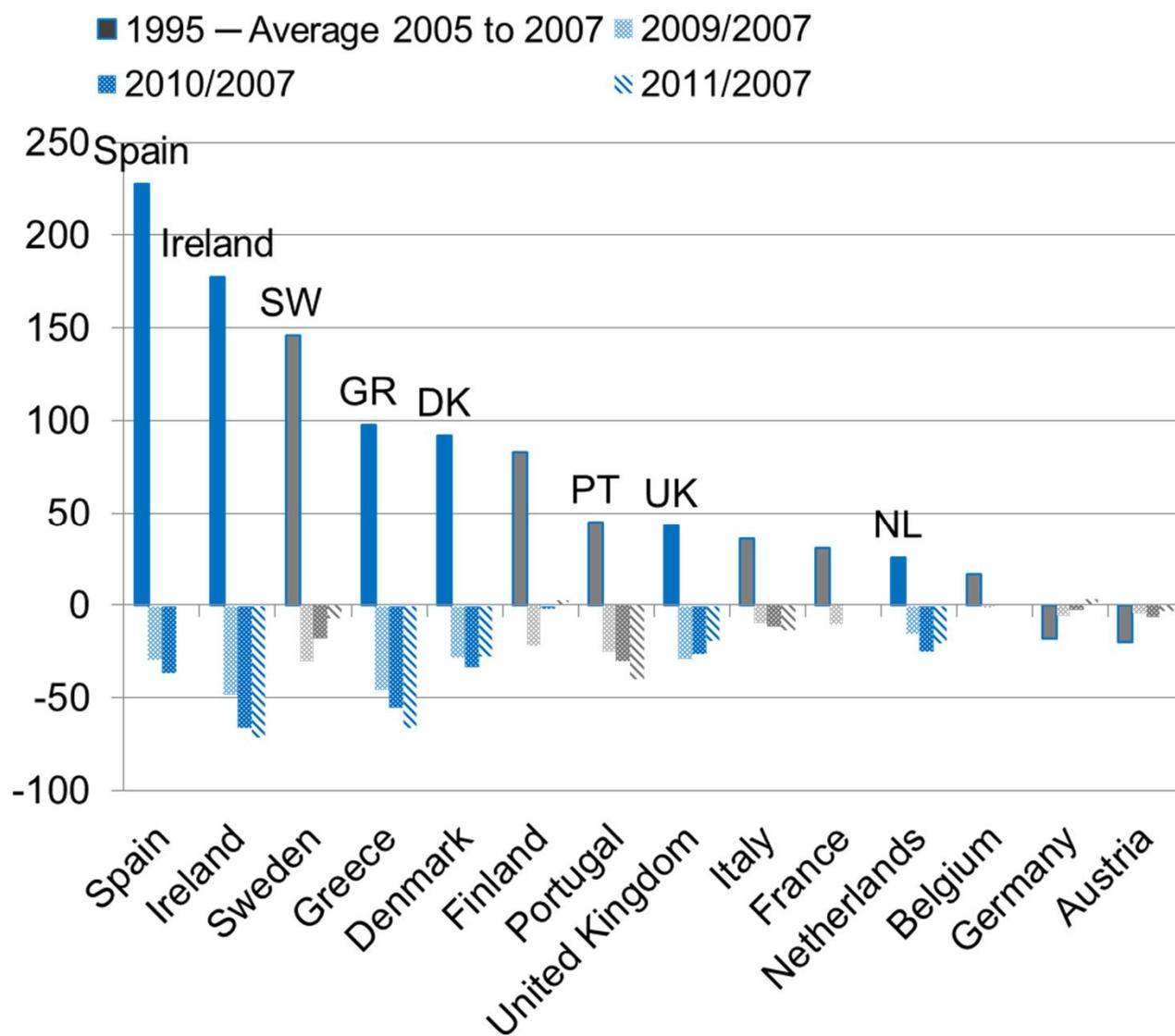
Boom – NonBust :

FI, SW, FR, BE

NonBoom :

IT, PT, AT, GE

# Change in Real Residential Investment (in %)



➤ *Double Bubble*  
ES, IR, GR, DK

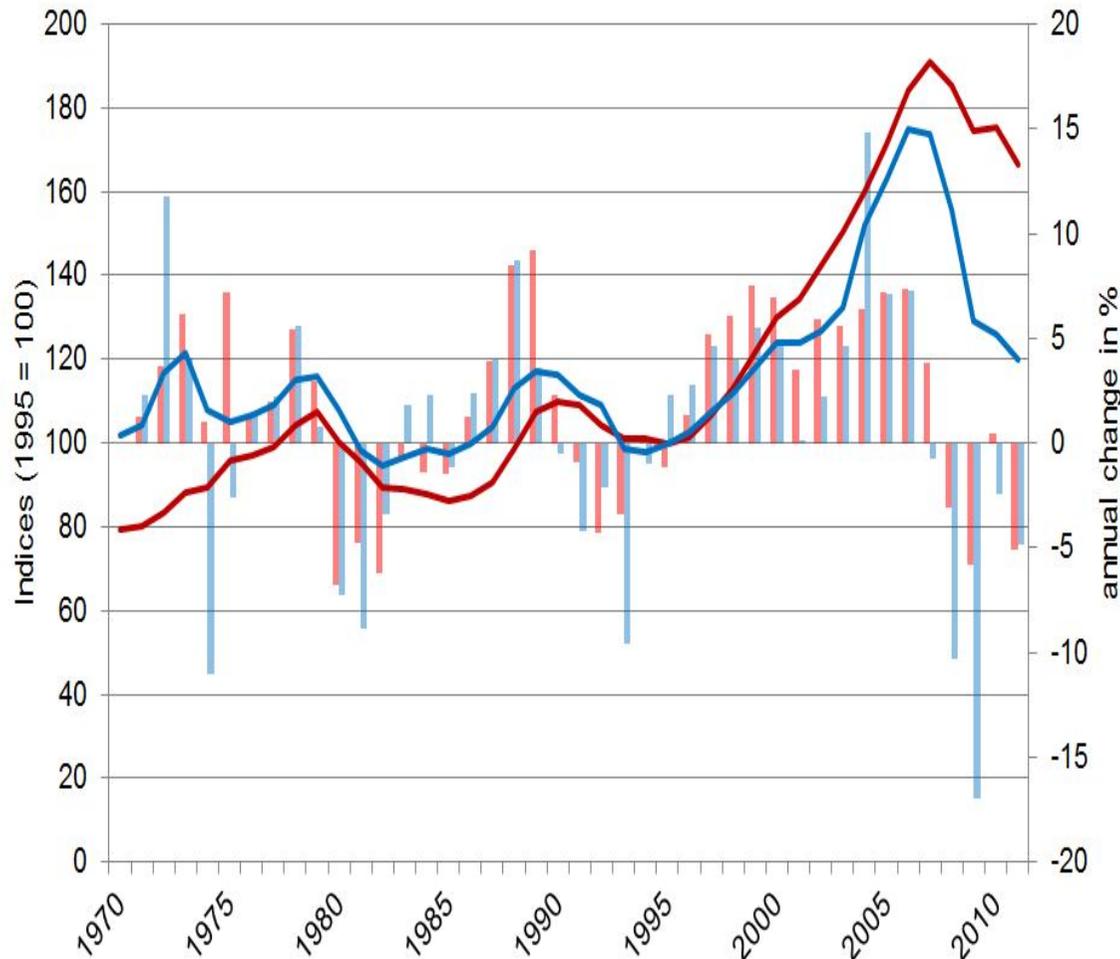
➤ UK: rather low level of house building even during house price boom (HI/GDP betw. 1995 and 2009: 3.1% on average; EU-14: 5.4%)

➤ Sharp drop in output even in countries with no supply overhangs  
SW, NL, PT

— > Lower levels of house building are helping to keep up prices of existing homes !!

# The ongoing EU-14 housing market cycle in hist. perspective

Real House Prices (—) and Real Housing Investments (—) unweighted average of EU-14



(1) Historically (1970–1994):

- real HP trend with an av. growth rate of 1% p.a.
- Corr. (HP/HI): + 0.64

(2) Ongoing Cycle (1995–2011–?):

- very long (12 years up; 5 years down to date)
- av. gr. rate HP: 3.3% p.a.
- Corr. (HP/HI): + 0.84

=> House Prices now more representative for overall housing market performance!  
 - > Home ownership rate up from 57% (1980) to 64% (2009)

(3) Downswing (2007 – 2011):

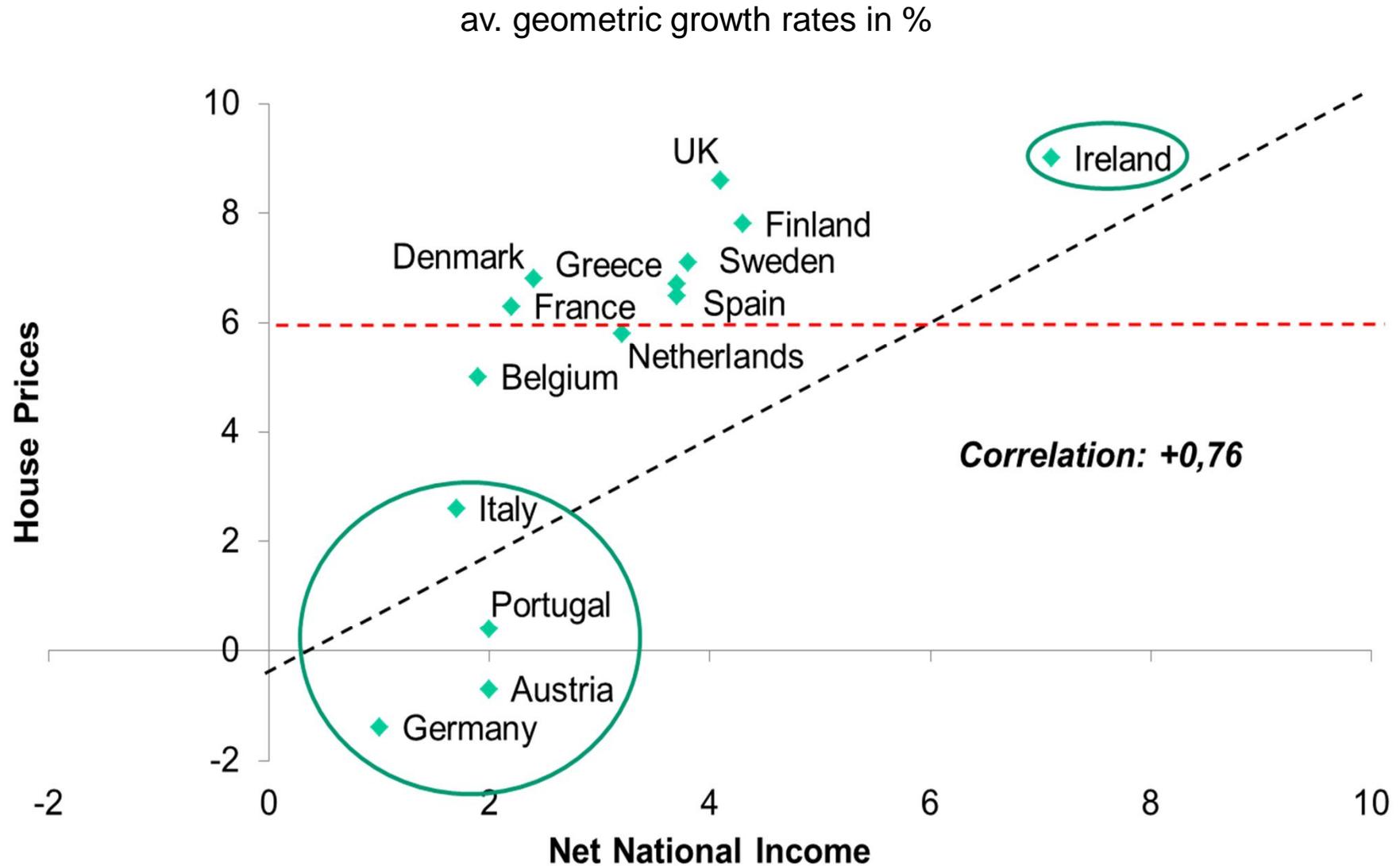
- much stronger drop in real HI compared to real HP

=> Macroeconomic policies more successful in stabilising HP than HI !!

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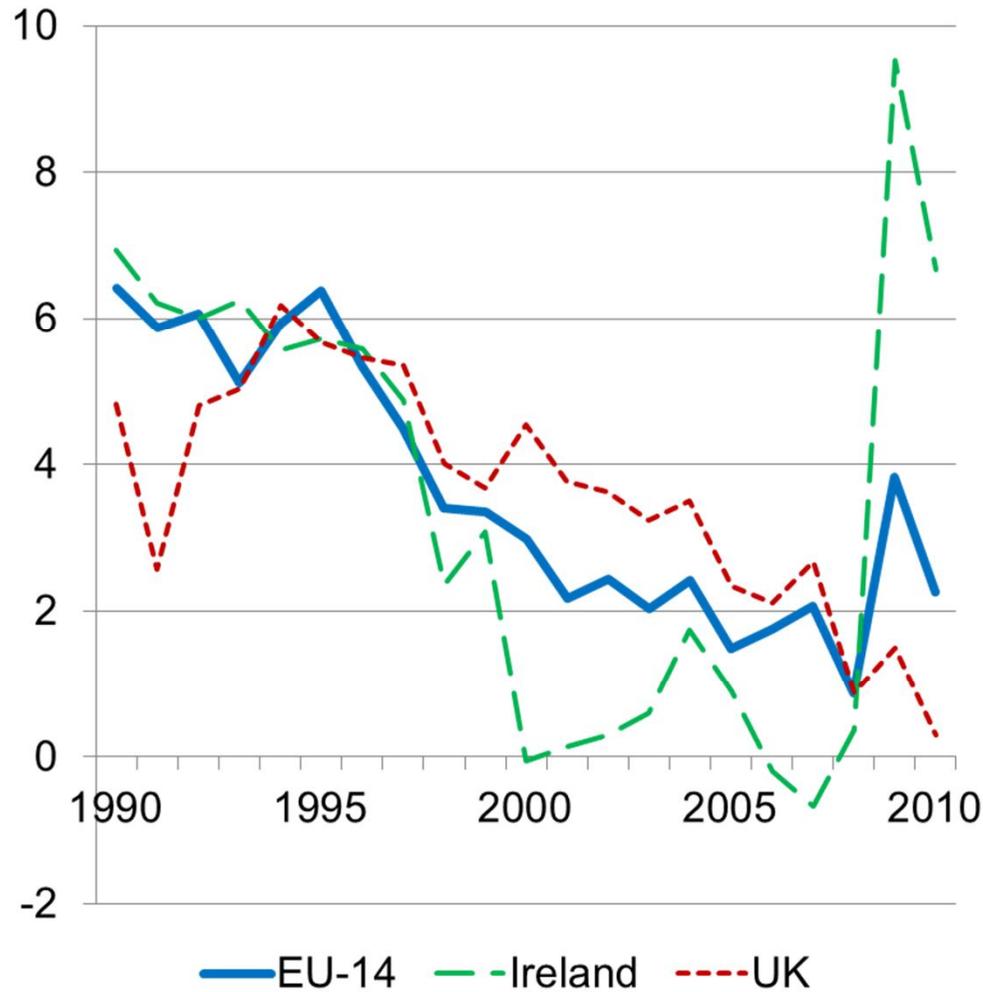
# Macroeconomic Fundamentals

# Real House Prices vs. Real Income Growth (1995 – 2007)

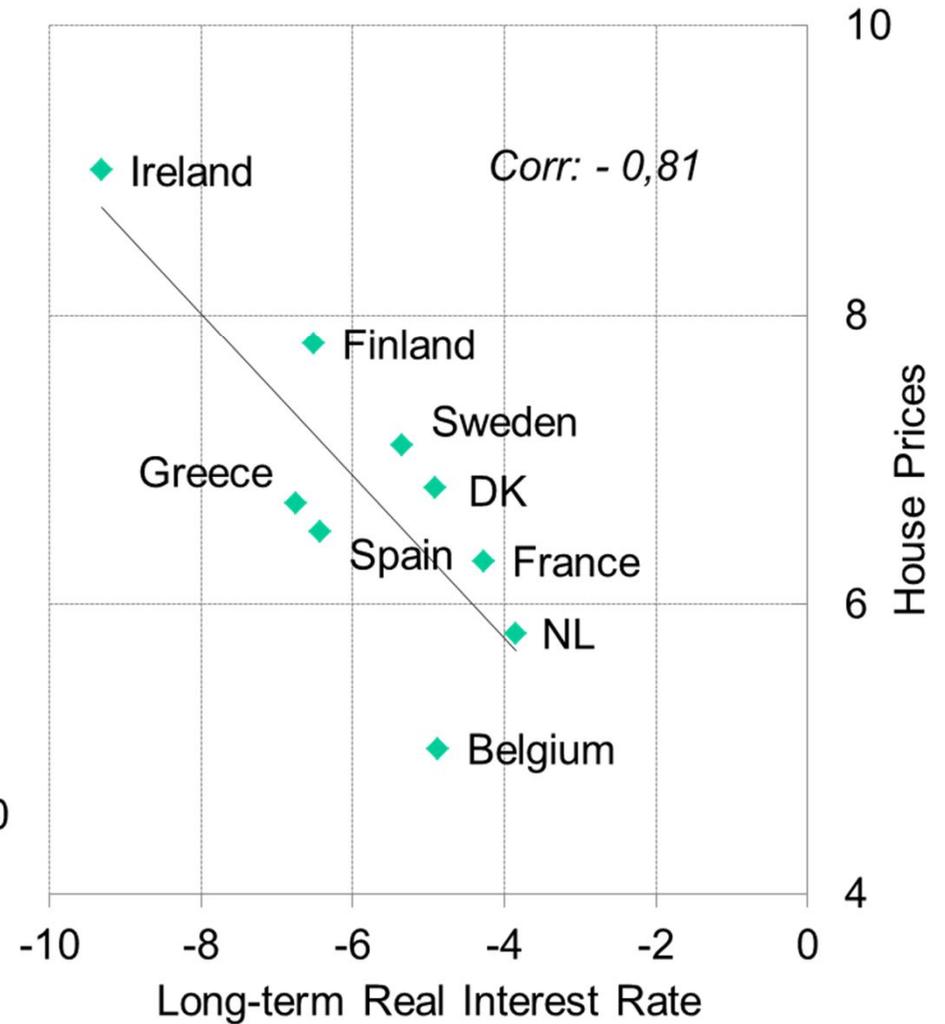


# Real House Prices vs. Real Interest Rates

Long-term Real Interest Rate (%)



Average Annual Change in Boom Markets (%) (1995–2007)



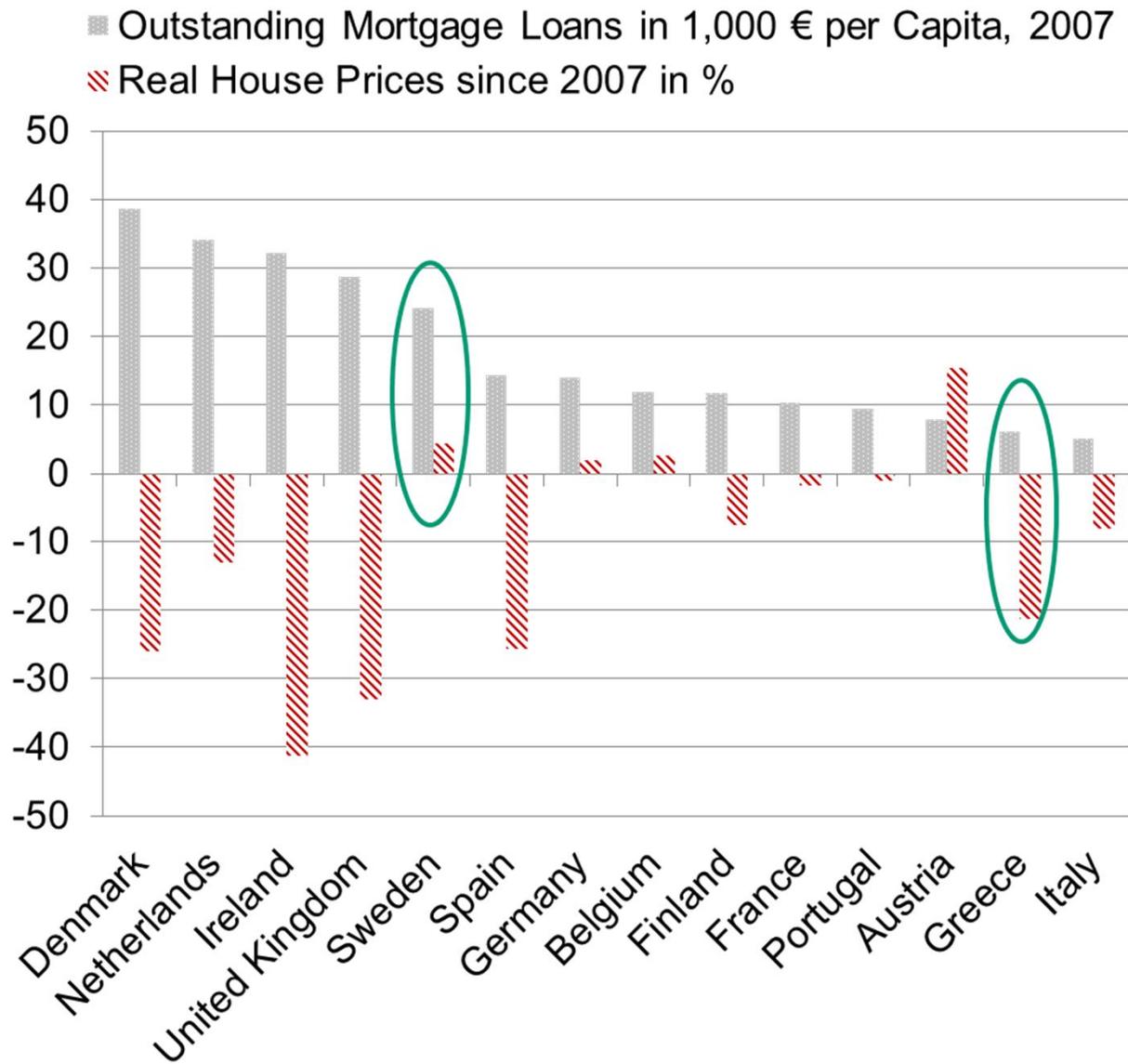
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# Country-specific Institutions

# A Characterisation based on Financial Market Indicators

|                             | Financial Reform Index 1995<br>(Abiad et al. 2008) | Mortgage Market 'Completeness' 2008 (IMF, 2008) | Mortgage Backed Securities / Outstanding Mortgage Loans – Av. 2003 to 2006 (EMF-Hypostat, 2004, 2005, 2006,2007) | Share of variable rate loans (ECB, 2003) | Typical Loan-to-Value (LTV) Ratio (ECB, 2003 a. o.) | Level of Household Debt (Eurostat) | Growth of new loans for house purchase (ECB, 2009) | Typical loan maturity (ECB, 2003 a. 2009; a.o.) |
|-----------------------------|--|---|--|--|---|------------------------------------|--|---|
| <b>Boom-Bust markets</b>    |  |   |  |  |   |                                    |  |   |
| Denmark                     | +++  | +++   | --   | -  | ++  | +++                                | -  | 30  |
| Greece                      | n.   | o   | ++   | +++                                      | o   | --                                 | +++  | 15-20   |
| Ireland                     | +++  | +++   | +++  | +  | --  | +++                                | ++   | 31-35   |
| Spain                       | +++  | ++  | ++   | ++                                       | --  | +                                  | +  | 30  |
| United Kingdom              | +++  | +++   | +++  | ++                                       | o   | ++                                 | o  | 25  |
| As a group                  | +++  | +++   | +++  | ++                                       | -   | ++                                 | ++   | 27  |
| Netherlands                 | +++  | ++  | ++   | +  | +++   | +++                                | +  | 30  |
| <b>Boom-NonBust markets</b> |  |   |  |  |   |                                    |  |   |
| Belgium                     | o  | o   | o  | ---                                      | ++  | -                                  | o  | 20  |
| Finland                     | -  | ++  | o  | +++                                      | o   | o                                  | o  | 20-25   |
| France                      | +++  | ---   | -  | --                                       | o   | o                                  | o  | 19  |
| Sweden                      | +++  | +++   | --   | o  | ++  | +                                  | +++  | 25  |
| As a group                  | +  | +   | -  | -  | +   | o                                  | +  | 22  |
| <b>NonBoom markets</b>      |  |   |  |  |   |                                    |  |   |
| Austria                     | --   | -   | ---  | o  | ---   | -                                  | o  | 25  |
| Germany                     | o  | --  | --   | ---                                      | --  | -                                  | ---  | 25  |
| Italy                       | -  | --  | +  | +  | ---   | --                                 | +  | 15  |
| As a group                  | -  | --  | --   | -  | ---   | -                                  | -  | 22  |
| Portugal                    | n.   | n.  | +++  | +++                                      | n.  | ++                                 | o  | n.  |

# House Price Change vs. Private Household Debt



## Theory:

- Not *Gross Debt*, but *Net Wealth* counts
  - However, *Net Wealth* developm. depends on HP developm. and leverage
  - HP and Debt interactive !
- ⇒ *Gross Debt* important when HP are declining

## Empirics:

- Strong relationship betw. scale of household debt in 2007 and real HP developm. after 2007 (exc.: SW, GR)
- Macroeconomic policies can help:
  - monetary easing; fiscal transfers to households; tax relief, etc...
  - However, limits to rate cuts and limits to government debt

# A Characterisation based on Housing Policy Indicators

|                             | <b>Capital Gains Taxes</b> (own calc. based on nat. information) | <b>Value of Mortgage Interest Tax Relief</b> (OECD, 2011) | <b>Transaction Costs of Purchasing Property</b> (EMF, 2010) | <b>Rent Regulation Index</b> (own calc. based on nat. information; broadly in line with OECD, 2011) | <b>State Subsidies for Housing</b> (Eurostat) | <b>Share of Social Housing in total stock</b> (Housing in Europe, 2011) | <b>Home owners Quote</b> (Housing in Europe, 2011) |
|-----------------------------|--|---|---|---|---|---|--|
| <b>Boom-Bust markets</b>    |  |   |   |   |   |   |  |
| Denmark                     | +++  | +++   | ---   | 0   | 0   | ++  | ---  |
| Greece                      | 0  | +++   | +++   | ---   | n.  | ---   | ++   |
| Ireland                     | 0  | 0   | --  | ---   | +++   | 0   | +++  |
| Spain                       | -  | +   | ++  | -   | +++   | ---   | +++  |
| United Kingdom              | ---  | ---   | ---   | ---   | 0   | ++  | +  |
| As a group                  | 0  | ++  | -   | --  | ++  | -   | ++   |
| Netherlands                 | ---  | +++   | -   | -   | ++  | +++   | 0  |
| <b>Boom-NonBust markets</b> |  |   |   |   |   |   |  |
| Belgium                     | --   | +   | 0   | ---   | --  | 0   | +  |
| Finland                     | +  | ++  | 0   | -   | --  | +   | 0  |
| France                      | --   | 0   | +++   | -   | +++   | +   | -  |
| Sweden                      | ++   | ++  | --  | +++   | +   | +++   | --   |
| As a group                  | -  | +   | +   | -   | 0   | ++  | -  |
| <b>NonBoom markets</b>      |  |   |   |   |   |   |  |
| Austria                     | +++  | --  | 0   | -   | 0   | +++   | --   |
| Germany                     | +++  | ---   | -   | -   | ++  | -   | ---  |
| Italy                       | ++   | --  | ++  | +++   | +   | --  | ++   |
| As a group                  | +++  | --  | +   | +   | +   | 0   | -  |
| Portugal                    | +  | -   | +   | +++   | n.  | --  | +++  |

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# Conclusions

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## (1) Broadly common factors in boom countries:

- historically low (real) interest rates
- strong growth in real disposable income and good income expectations
- a mutually reinforcing relationship between house prices and mortgage lending

These factors led to:

- a strong demand for housing services and mortgages
- a stronger synchronisation of house prices during the period 1999 – 2007
- a higher trend growth of house prices
- an investment boom in some countries

## Conclusions

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(2) A combination of factors contributed to house price busts after 2007:

- high owner-occupation rate (IR, ES, UK, GR)
- high level of personal debt (IR, ES, UK, NL)
- dominance of variable interest rate mortgages (IR, ES, DK)
- intensive use of *Securitisation* and new capital-market based refinancing instruments (ES, UK, NL, IR)
- problems of overall competitiveness and the over-representation of construction in the economy → supply overhangs (IR, ES)

## Conclusions

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(3) Some factors helped to avoid a large (or even larger) decline in house prices:

- predominantly fixed rate mortgage lending (BE, FR, NL, GE)
- reasonable loan-to-value ratios (FR, FI, IT, GE, AT)
- more weight on traditional refinancing instruments (BE, FR, GE, AT)
  
- a reasonable mixture of housing tenure (SW, NL, GE, AT)
- a high share of social housing (FI, FR, SW, AT)
- strong housing-related fiscal stimulus (FR) or tax policy changes boosting demand for housing (SW, FR, NL)
- a high share of outright ownership (PT, IT)
  
- local housing supply problems due to land shortages and/or high building costs (UK, SW, FR, NL)

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THANK YOU