Housing Markets and the Global Financial Crisis

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“I THOUGHT WE WERE JUST BUYING A HOUSE!”

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US Power Rising

1. Absence of constraint equals: US global financial arbitrage / $ recycling
   - The US escaped the usual constraints, ‘91-05
     - Over-consumed (from 65% to 70% of GDP)
     - Overinvested at home (GFCF from 14% => 19%)
     - Overinvested overseas ($7 trillion gross)
   - And made money doing this! 😊
     - At the cost of rising net foreign debt... 😞
US Power Rising

1. Absence of constraint

2. Control over production chains
   - US owned share of MSCI from 10% => 24% vs. Foreign Share of US from 5% => 9.7%
   - US MNCs’ share of GWP up 40% => 7.8%
   - Ratio of USDIA to FDIUS, 1995-2004
     - Assets ratio from 1.32 => 1.5
     - Value added ratio from 1.4 => 1.6
     - Turnover ratio from 1.1 => 1.4
US Power Rising

1. Absence of constraint
2. Control over production chains
3. Differential growth
   • “market share” not absolute growth
   • US share of OECD GDP up 4.2 % points to 42.7%, 1991-2005 (vs fall from 46.6% [1950] => 37.8% [1982])
   • US share of world GDP stable at 20% despite rapid growth in China, India, etc
The 1990-2000s US growth cycle

Disinflation

Asia Recycles US Dollars as New Mortgage Debt

Housing Finance System

↑ Tax revenue

More Consumption

Faster US Economic Growth

US trade deficits

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Housing finance

- High rates of homeownership +
- High levels of mortgage debt to GDP +
- Easy refinance of mortgage debt and home equity withdrawal +
- Securitization of mortgages

= “US style housing market”

can create (or destroy) lots of aggregate demand

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Housing wealth

• New homeowners buying between 1999 and 2005 saw an increase in median net wealth from $11,100 to $88,000, mostly in home equity

• Incumbent households’ median net wealth nearly doubled from about $152,400 to $289,000

• People spent this money, powering economy
MEW vs GDP, 1996-2006

GDP Growth: With and Without Mortgage Equity Withdrawal

Percent Real GDP Growth

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Employment gains, 1991-2005

Share of OECD Population, 2005, %
Share of New Jobs, %

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## Differential growth (adjusted)

<table>
<thead>
<tr>
<th>Population adjusted % change, 1991-2005</th>
<th>USA</th>
<th>OECD Ave.</th>
<th>FRG</th>
<th>Japan</th>
</tr>
</thead>
<tbody>
<tr>
<td>GDP (real, local currency)</td>
<td>33.5</td>
<td>28.1</td>
<td>17.3</td>
<td>13.3</td>
</tr>
<tr>
<td># of Employed</td>
<td>1.8</td>
<td>3.0</td>
<td>-2.9</td>
<td>-2.7</td>
</tr>
<tr>
<td># of Unemployed</td>
<td>-24.8</td>
<td>6.8</td>
<td>91.5</td>
<td>109.7</td>
</tr>
<tr>
<td>GFCF</td>
<td>79.9</td>
<td>48.2</td>
<td>2.7</td>
<td>-13.5</td>
</tr>
<tr>
<td>GFCF Metals/Mach</td>
<td>159.8</td>
<td>100.1</td>
<td>19.0</td>
<td>22.8</td>
</tr>
</tbody>
</table>

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Four types of housing regimes defined by relative deviation from the average OECD levels of mortgage debt to GDP and owner-occupation prevailing 1992 to 2002 (in percentage points)
Mortgage Debt Outstanding (percent of GDP)
Ratio of US Housing Prices to Income – the fundamental issue

Cost of buying actually fell in 1990s => more buying

2006 price peak

http://calculatedrisk.blogspot.com/
House price-to-income ratios*

Ratio
6

Australia  Britain
Ireland  Canada
New Zealand  US

* Various combinations of median and mean measures of house prices and incomes used depending on availability.

Source: ABS; BEA; BIS; CLG; CSO; OECD; ONS; RBNZ; REIA; Statistics Canada; Statistics NZ; Thomson Financial
Economies at risk – where housing growth is not explained by economic growth

Fundamental drivers of house prices are modelled as: the lagged ratio of house prices to disposable incomes, growth in disposable income per capita, short-term interest rates, long-term interest rates, credit growth, and changes in equity prices and working-age population.

Source: IMF Staff calculations, World Economic Outlook, April and October 2008
## Political Time Horizons, Property Booms, and Financial Liberalisation

<table>
<thead>
<tr>
<th></th>
<th>Short</th>
<th>Long</th>
</tr>
</thead>
<tbody>
<tr>
<td>Public</td>
<td><em>Politicians</em></td>
<td><em>Regulators</em></td>
</tr>
<tr>
<td>Private</td>
<td><em>Banks</em></td>
<td><em>Homeowners &amp; Citizens</em></td>
</tr>
</tbody>
</table>
Changing Housing Markets in Australia and Denmark

- Taxation is a national concern

- Financial deregulation and reregulation is transnational

- Groups fight for credit access within and between generations
House price-to-income ratios*

Various combinations of median and mean measures of house prices and incomes used depending on availability

Source: ABS; BEA; BIS; CLG; CSO; OECD; ONS; RBNZ; REIA; Statistics Canada; Statistics NZ; Thomson Financial

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Changing Housing Markets in New Zealand

• Financial liberalization during the 1980s and 1990s aimed to produce an ‘asset-based society’

• But reforms created a generational split between housing market ‘insiders’ and ‘outsiders’

• The rate of home ownership fell from 74% in 1991 to 67% in 2006, and is predicted to fall below 62% by 2016

• Home ownership in the 25-44 age group declined by 44% between 1991 and 2001
Changing Housing Markets in New Zealand

• In the recent property boom policymakers faced a monetary ‘catch 22’:
  – Interest rates were raised in an attempt to ease the property bubble
  – But borrowers’ preference for fixed-term interest rates created a time lag
  – Higher interest rates attracted more foreign capital and pushed up the value of the NZ$
  – This fuelled consumption, inflation, and a worsening trade deficit

• The impact of the global financial crisis has impeded the impact of interest rate cuts, and constrained the scope for further fiscal stimulus
Questions?