

Proposal for Parallel Session 2A: House Price Movements and the Economy

Credit, Housing Collateral and Consumption: Evidence from the UK, Japan and the US

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Abstract of Current Paper

The contrasting consumption behaviour of UK, US and Japanese households is examined in this paper through the lens of modernised Ando-Modigliani style consumption functions. Income growth expectations are treated systematically and income uncertainty and credit channel features are incorporated. These models therefore capture important parts of the financial accelerator. The evidence is that, since 1980, credit availability for UK and US but not Japanese households has undergone large shifts. Moreover, there is UK and US evidence both for a shift in the average consumption to income ratio as down-payment constraints eased, and for a shift in the collateral role of housing wealth as home equity loans became more freely available. Point estimates suggest the housing collateral effect is larger in the US than the UK, while land prices in Japan still have a negative effect on consumer spending. Together with evidence for negative real interest rate effects in the UK and US and positive ones in Japan, this suggests important differences in the transmission of monetary and credit shocks.

Plan for Improvements Before the 2010 IARIW Conference

Between now and the spring of 2010, we plan to improve this paper in three major ways. First, we will add an appendix showing why an Euler-approach to estimating consumption functions with only stationary variables (usually log-first difference variables) is empirically rejected in the three countries that we examine. Secondly, we will address potential simultaneity in our specifications by replacing income with forecasted income in some models. Preliminary work along both of these dimensions has been very favourable, and we have good reason to anticipate that a future version of this paper would provide even more convincing results. Finally, to shed more light on a topic of interest to the IARIW, we plan to add a section which quantifies how recent reductions in household wealth and credit availability are likely to affect the personal saving rate in the U.S. and UK, and which discusses potential spill-over effects on trading partners such as Japan.