

DANMARKS NATIONALBANK

20 FEBRUARY 2019 — NO. 2

Fluctuations in house prices affect consumer spending and borrowing

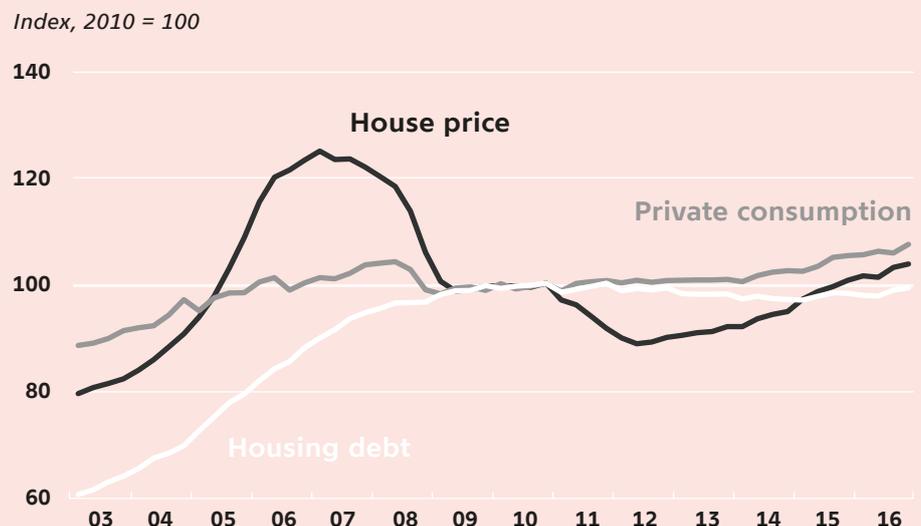
Homeowners increase their borrowing and spending when house prices rise

Many Danish homeowners convert rising house prices into spending by increasing their mortgage debt. They do this by refinancing existing mortgages or raising additional loans, thereby translating home equity into liquid funds. Rising prices of owner-occupied homes thus provide scope for increased consumer spending or e.g. repayment of other debt.

That is the conclusion of a study published as a working paper. Detailed data at household level have made it possible to analyse developments from 2009 to 2016.

The well-known Danish mortgage credit system plays an important role when homeowners convert their home equity into spending. The mortgage credit system is based on the premise that mortgages are raised against the home as collateral and that there is a direct link between the mortgage and the underlying bonds. The right to repay mortgage loans at any time and the possibility of increasing the mortgage debt when house prices are rising ensure a certain degree of flexibility. It means that homeowners can use their home equity to e.g. adjust their spending over their lifetimes.

Spending and debt are affected by house price developments



Source: Statistics Denmark and own calculations. All series are shown in real terms.

A 1 per cent price increase for owner-occupied housing will increase home-equity extraction by 0.2 percentage point on average, and for each extra krone of home equity extracted, approximately one third will be spent financing current expenses such as consumption and home improvements. The analysis also shows that when house prices rise, homeowners with a high level of indebtedness and limited borrowing opportunities raise loans against home equity to a much higher degree than others.

The house price bubble and the financial crisis in the mid-2000s illustrated that house prices can rise and fall significantly. Another working paper looks at how unexpected house price changes can impact consumption. One of its conclusions is that Danish households increase their mortgage debt and spending when they find that their homes have appreciated more in value than expected. The relationship is amplified if the price of the home goes up at the same time as the interest rate on fixed rate mortgage loans goes down. This indicates that mortgage

refinancing has to be advantageous for homeowners by giving them an opportunity to lock in a new, lower interest rate before unanticipated housing wealth gains are translated into increased spending. This was seen e.g. in early 2015 when interest rates were falling while house prices and borrowing activity were rising.

Danmarks Nationalbank's objective is to ensure that Denmark has a robust economy. In Denmark, private consumption accounts for around half of the total Danish gross domestic product, and housing accounts for the largest share of the Danes' aggregate assets. Accordingly, it is important to know how house price fluctuations affect the Danes' spending and borrowing. For this reason, among others, Danmarks Nationalbank works with housing market analysis.

**See the two working papers ([link](#))
at Danmarks Nationalbank's website**

ABOUT NEWS



News are news articles based on analyses, working papers or other longer texts from Danmarks Nationalbank. News primarily

address journalists, politicians, government officials, specialists and others who want to be updated on current topics.

The news article consists of a Danish and an English version. In case of doubt regarding the correctness of the translation the Danish version is considered to be binding.

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This edition closed for
contributions on 19 February 2019



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