Dematerialising money: The ebb and flow of wealth between housing and other things

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Abstract

This paper considers mortgage equity withdrawal – a practice that is increasingly important for monitoring whole economies – from a housing policy perspective. We take the UK as a case study, because trends in housing finance, consumer behaviour and the governance of housing wealth make it an apposite example. We begin by offering a critique of data resources and by documenting the growing significance and changing style of mortgage equity withdrawal in the UK. We then to consider how secured borrowings are spent, identifying and accounting for a trend away from reinvestment in housing and towards the consumption of other things. We go on to suggest that this shift may be mediated by subjectively experienced, as well as objectively measured, neighbourhood effects. We conclude by weighing up the costs and benefits of ‘wealth effects’ and ‘equity leakage’ for both housing and economic policy.
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Introduction: ‘Wealth effects’ vs. equity ‘leakage’

There is a considerable (mainly economics) literature addressing the implications of housing wealth for the consumption of other things. Case, Quigley and Schiller (2005), for example consider the link between housing wealth, financial wealth and consumption using annual data from a panel of 14 countries over 25 years as well as a panel of US states observed quarterly during the 1980s and 1990s. They find ‘a statistically significant and rather large effect of housing wealth upon household consumption’ (p. 1). To some extent these wealth effects are driven by people’s perceptions and experiences of movements in house prices. But while perceptions of shifts in asset values must play a part in determining how much people spend from any part of their wealth portfolio, a key mechanism translating housing wealth into consumer spending is housing equity withdrawal (HEW). In this paper we are concerned with one element of this, namely mortgage equity withdrawal (MEW). This is because, in economies increasingly driven more by credit than cash, secured borrowing has become the easiest and (by some measures) cheapest way to raise the funds for a very wide range of spending. As a consequence, housing wealth, which has traditionally been regarded as a fixed asset, is increasingly fungible: it is no longer trapped in bricks and mortar; it can readily be rolled out and spent on other things.

The consumption effects of housing wealth are especially notable for the UK, in ways documented by Smith (in press, a). In this paper we focus on the distinctive case of the UK, and use it to consider some questions about the wealth effects of owner occupation which are rarely asked in a literature pre-occupied with the economic, rather than housing policy, implications of equity withdrawal. In particular we point out that the kinds of MEW which, from an economic perspective may be experienced as a protective boost to consumption, might, from a housing perspective, signal a risky drain on the quality and condition of the stock.
There discussion is in three parts. In the first section we offer a roundup of the data resources appropriate to this exercise, and document empirically the growing significance and changing style of housing equity withdrawal in the UK. Next we consider what that housing equity is spent on, paying attention to patterns of reinvestment in housing and raising questions about the character of that investment. Finally we expose a trend towards spending housing wealth on other things, and so begin to weigh up the costs and benefits of ‘wealth effects’ versus ‘equity leakage’.

**Spending the home**

In this section we offer a round-up of the main sources of data on MEW in the UK. We explain why household survey data have a number of advantages over the Bank of England’s aggregate statistics, and concentrate our efforts accordingly. The British Household Panel Survey (BHPS), the Family Resources Survey (FRS) and the Survey of English Housing (SEH) all yield information on gross mortgage equity withdrawal to flesh out trends and provide a finer grained overview of the way equity withdrawal works. All of these surveys are extensive, have some kind of random base, and are conducted annually (though their runs are still short compared to the length of time most owners hold mortgages). Table 1 summarises their key characteristics.

Each of these surveys has some important strengths, and some notable limitations, as ways of documenting MEW. In the full paper we explore these in some detail. Our broad conclusion is that as far as documenting mortgage equity withdrawal is concerned, the BHPS contains the most consistent run of data, but perhaps the least useful questions; the FRS has the best questions at times, but a patchy run, and the SEH has some notable gaps, but in its most recent sweep is exhaustively comprehensive if rather difficult to navigate.

Notwithstanding these caveats, we show in the paper that, individually and in combination, these data signal some important trends that both confirm and add to the scene set by the Bank of England’s figures. In describing these trends we draw both on our own analyses and from related work by Banks et al. (2004), Bridges et al. (2005), Benito and Power (2004), Benito and Wood (2005), Case et al. (2005),
Campbell and Cocco (2005), Disney et al. (2005), and Smith and Vass (2004). From this we offer three generalizations from these surveys about trends in mortgage equity withdrawal. In the full paper we include a number of figures to illustrate these findings.

First, there is evidence of a steady growth into and beyond the millennium in the size of the sums released in situ through MEW. Second, these surveys show a steady rise from at least the mid 1990s in the proportions of British mortgage holders who have increased their in situ secured borrowing. Third, the empirical evidence in the FRS and SEH (though not in the BHPS which does not contain appropriate questions) testifies to the increased diversity of routes for equity extraction, and more crucially to the changing balance of these in households’ accounts. While the data are patchy, all indications are that the balance is shifting towards MEW and away from HEW, away from overmortgaging towards in situ drawdown, and with a preference on the latter to take a further advance rather than go to the effort of remortgaging (except, perhaps where this marks a change from less to more flexible products (Smith et al. 2002)).

Taken together, then, a range of extensive surveys signal the growing importance in the UK of opportunities to draw so flexibly and routinely from housing equity – using mortgages as an interface – that housing wealth is effectively rolled into other considerations around households savings, investments, spendings and debt. Furthermore, whereas the indication is that equity released through trading-down and last time sales may be saved rather than spent; it seems that the more modest sums, of around £20k per event, that are withdrawn at the point of remortgage, further advance or flexible drawdown (what we are calling in situ MEW) are more likely to be spent than saved (Benito and Power 2004).

The question is, what is this wealth spent on and, critically, among owner occupiers – the individuals responsible not just for the buoyancy of the high street but also for the maintenance, repair and improvement, the sustained quality and condition, of the largest segment of the housing stock – how much is reinvested and how much flows into other areas of the economy?
Changing rooms?

The UK has an old and aging stock of housing. Reinvestment into existing dwellings is a key means by which the quality, condition and future of the residential environment is secured. Interestingly, successive governments have made it clear that where the majority of housing – owner occupation – is concerned, it is the responsibility of individual owner-buyers to make this investment, not least because of the asset value of their homes:

‘It is neither possible nor desirable to provide public money to tackle all the problems of poor condition housing in the private sector’ (DETR 2000a, 39-40)
‘It is only right that the responsibility for maintaining privately owned homes, which for many people is their most valuable asset, should be first and foremost with the owner’ (DETR 2001, 9)
‘Responsibility for these homes must rest first and foremost with the homeowner’ (ODPM 2003b, 5).

There is clearly a presumption that at least some part of any equity extracted from homes will be reinvested into them: as Groves and Sankey (2005) have argued, this practice has considerable potential for securing the future of the private housing stock. Yet there is no substantial regulation of this by the state or the market (lenders), there are no specific guidelines issued by national or local governments, and there is little obvious interest in any part of the system in the prospect, or problem, of ‘equity leakage’. It is, then, only the owners themselves that we can turn to, in order to discover what happens.

Accordingly, in this section, we interrogate the BHPS, SEH and FRS for insights on trends in and patterns of spend from housing equity, through in situ MEW. As other commentators have noted, it is not that easy to use standard survey data to ascertain how MEW is spent (Farlow 2005). We therefore juxtapose information from the most recent sweeps of these surveys, with evidence from two smaller but more targeted surveys in order to offer some pointers on what shapes these behaviours. The first of these smaller surveys (CML/BoE) spoke to just over 900 British mortgage holders during 2000, documenting just over 1,000 equity withdrawal events (Davey 2001; Davey and Earley, 2001). (This is the only one of the surveys that we have not analysed ourselves, drawing instead from the published reports.) The second is a
survey of 486 flexible mortgage holders (FMS) in England conducted in 2001 (Smith et al. 2001).

The surveys are variously and unevenly geared to issues around reinvestment and equity leakage, and this is detailed in the full paper. By stitching the sometimes-fragmentary accounts from all five surveys together, we offer three observations.

First there is a strong inclination among all survey respondents to reinvest their extracted housing equity back into their homes: two-thirds to three-quarters of those who engage in MEW spend at least some of it on home repairs, improvements or extensions.

Second, notwithstanding the dominance of the reinvestment theme, it is not always clear what this means to households. While the surveys all document several categories of spend around consumption goods and welfare needs, the tools are rather blunt. Sharpening them up with reference to related, qualitative research raises the possibility that even when it looks as if spend is directed into property (even when people experience their spend as being of this type), it may not constitute ‘reinvestment’ sensu stricto. Instead housing equity may be flowing out of the built environment and into other things – into items which are perceived to add financial value but which may not maintain or improve the use value (or long term condition) of the stock (Smith, in press b).

Third, and crucially, our analysis suggests that the balance of spend of MEW between homes and on other things may be changing. This trend is best-illustrated across the 13 sweeps of the BHPS shown in figure 1. While 65 per cent households spent their MEW on home improvements in 1991, just 44 per cent were doing so by 2003. The proportion of those spending on home extensions also dropped by a nearly third, from 30 per cent to 22 per cent in that period, while the tendency to spend on cars, other consumer goods and other specified (but unrecoverable) reasons all increased. And although the numbers are small, a comparison of the five year periods 1994-8 and 1999-2003, shows that while households only reinvesting in the home doubled, those only spending on other things increased threefold. In the light of this, whereas the majority of analyses of, and discussion around, MEW behaviour concentrate on
predictors of who withdraws and who does not, our analysis points to the importance of considering what differentiates those who reinvest in their homes from those who spend on other things. This is the subject of the third part of the paper.

Dematerializing money…

While it is usual in studies of MEW to consider the question of who engages in additional borrowing and why, no studies that we are aware of have considered what influences the split between reinvesting in housing and spending on other things. MEW is usually, and surprisingly uncritically, presumed to be net of reinvestment, yet the truth is that not much is known about the way mortgage holders weigh the lure of the high street against the practicalities of conserving home assets (or spending them in other ways).

Elsewhere, we consider these ‘other ways’ more fully, noting particularly the extent to which housing wealth has a safety net or insurance role. To conclude the paper, however, we explore the possibility that the imperative to reinvest MEW in homes, or spend it on other things, is mediated by neighbourhood effects. Three of the surveys are helpful here: the BHPS contains a rich store of attitudinal data around home and neighbourhood, but carries no local geographical tag; the SEH contains a suite of attitudinal data, and is additionally tagged with ACORN codes; the FMS contains little attitudinal data but patterns of spend from housing equity have been linked by postcode to MOSAIC data. In examining this, we again focus on equity withdrawal in situ, targeting the kind of MEW that is not only increasing in prominence but which occurs only after some knowledge and experience of a home and/or neighbourhood environments have been acquired. Again we flag three findings.

First, there is mixed evidence of the extent to which engaging in MEW at all is contextualised by attitudes to home and neighbourhood. This mainly reflects the fact that most homeowners in the national surveys do not experience problems with their locality, have a high opinion of local services, and feel a commitment to where they live. If there is a trend it is, intriguingly, that people who withdraw housing equity are less rather than more enamoured with their locality than others. This raises a salient question: are they using this equity to arrest decline, improve environments and
enhance attachment to them? Or are they more inclined to compound their
detachment by spending their equity elsewhere, on other things?

Second, following this up, we find some evidence that people’s experience of
neighbourhood mediates the direction of spending from MEW; neighbourhood
variables impact on the extent to which borrowers spend housing equity on the home
or direct it to other things. This is a complex, at times paradoxical set of findings
which draw attention to two kinds of reinvestment: the kind that expresses local
commitment and aims for long term returns on housing quality and condition; and the
kind that maximises short term price gains, possibly prioritising GLAMS over
guttering.

Finally we consider whether more objective census based measures of neighbourhood
type (ACORN, for the SEH and MOSAIC for FMS) shed any light on how secured
loans are spent. We classify neighbourhood types according to whether interviewees
who live in them tend to spend some equity on their home, or all of it on other things.
This broadly descriptive approach provokes some interesting observations about the
contextual effects of MEW.

To take one example, there are eighteen MOSAIC neighbourhoods in which
households in the FMS are most likely to spend the proceeds of MEW on something
other than their home. The modal type among neighbourhoods prone to equity
leakage is described in MOSAIC as ‘close to retirement’: neighbourhoods whose
residents engage in consumption ‘as a means of maintaining their lifestyle’, and who
are ‘major purchasers’ of personal services, alongside homes and gardens accessories.
The two other neighbourhood types in contention here are: ‘high technologists’ who
show ‘little interest in DIY, gardening and other “home building” activities’ but will
‘spend large amounts to develop and maintain their lifestyle’; and ‘respectable rows’,
who ‘are measured in their hedonism’ but often find their spending is driven by
children’s needs. Here, then, are a group of neighbourhoods whose residents
experience multiple demands on their housing wealth and who may not (need, or be
able, to) prioritise reinvestment into the housing stock.
As a second illustration, consider the three, intriguingly contrasting, ACORN types in which the equity withdrawn by SEH interviewees is more likely to be spent on the home than on other things. These neighbourhood types are described as: ‘comfortably off’, ‘moderate means’ and ‘hard pressed’. The first accommodates ‘the home owning, stable and fairly comfortable backbone of modern Britain’. These are people who may not be wealthy but have few financial worries and for whom respectability is epitomised in the world of homes and gardens. They are, in effect, well motivated and financially able to access secured loans and to reinvest them in property.

Neighbourhoods of ‘moderate means’ often have high concentrations of former council housing – properties which may demand investment, and be an obvious first call on mortgage equity. The third neighbourhood type contains a mix of poorer households who are described as having limited opportunity to improve their economic circumstances. A possibility here is that securing the future financial value, as well as immediate utility, of owned homes is, for people in these settings, seen as the one viable route to social mobility.

The steer from the fuller analysis is that it could well be worth thinking more systematically about the many locational and neighbourhood factors which contextualise the way MEW is spent. A complex legacy of spatial differentials in house price appreciation already makes for marked differences in how much equity is stored in different parts of the housing stock. What we are suggesting is that there is an equally complex geography to the way that wealth is spent. The analysis undoubtedly raises as many questions as it answers, and in the end, a mix of methods – from the multilevel models that help disentangle compositional and contextual effects, to the qualitative inquiries required to make sense of them – will be needed to move the arguments on. What seems clear is that, as far as MEW is concerned, neighbourhood is a relevant variable, not just for understanding where housing wealth is concentrated, but also for appreciating how and why it is deployed.
Conclusion

This paper provides a snapshot of the ‘state of the art’ of MEW in the UK, in so far as it can be established from existing survey data. Specifically, it considers the quantity, quality and texture of the data available to address, from a housing policy perspective, questions that are more usually viewed through the lens of economic management.

From an economic point of view, key questions surround the magnitude overall of housing equity withdrawal (HEW); the size of the wealth effect, how it compares with the (consumption) effects of other kinds of wealth-holding, and the extent to which it boosts high street spending. From a housing policy perspective, on the other hand, a key concern is the extent of mortgage equity withdrawal: its impact on the financial sustainability of owner occupation and on the environmental sustainability of the national housing stock. The question here is not just how much people spend, but, crucially, what proportion of it they reinvest in their homes.

All the indicators we have considered point to a sustained and possibly increasing flow of equity out of housing and into other things. Whether this is a one-off bonanza, whether it is viable in the long term, how uneven is its impact, how unequal its effects, all remain to be seen. We have considered some of the factors that might influence key patterns, and there is scope to extend this line of analysis, particularly if key survey instruments begin to pick up more systematically on changing trends in housing finance. However, the analysis also raises a set of issues around the motivations, beliefs and behaviours of households which – whether to inform the stylised facts of economics or to enlarge the canvas of housing interventions – demand the texture that only a more qualitative enquiry can build up. This is the subject of ongoing work.
Acknowledgements

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References


Smith, S. J. (in press b) Owner occupation: at home with a hybrid of money and materials, Environment and Planning A.

Table 1: Monitoring trends in mortgage equity withdrawal among British households

<table>
<thead>
<tr>
<th>Survey</th>
<th>Period</th>
<th>Numbers (Average, pa)</th>
<th>Information on housing finances:</th>
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<tr>
<td></td>
<td></td>
<td>Interviewed</td>
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<tr>
<td>BHPS</td>
<td>1991-2003</td>
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<td>8,784</td>
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<td>FRS</td>
<td>1994-2003</td>
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<td>14,754</td>
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<tr>
<td>SEH</td>
<td>1998-2003</td>
<td>29,311</td>
<td>13,804</td>
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<th>Survey</th>
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<tr>
<td></td>
<td>Overmortgage</td>
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<tr>
<td>BHPS</td>
<td>No</td>
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</table>

1 Start date refers to the first sweep containing questions pertaining to mortgage equity withdrawal.
2 Combines mortgages on all owned properties (including second homes/ buy-to-let and so on)
<table>
<thead>
<tr>
<th></th>
<th>FRS</th>
<th></th>
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<tr>
<td></td>
<td>No</td>
<td>Yes</td>
<td>Yes, by</td>
<td>Yes, by</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>value</td>
<td>value (top-up, 1994-1996 only)</td>
</tr>
<tr>
<td>SEH</td>
<td>Yes in 2003, otherwise imputed from small nos.</td>
<td>Yes</td>
<td>Yes, but indicative until 2003</td>
<td>Yes (top up only, and indicative until 2003)</td>
</tr>
</tbody>
</table>
Figure 1: Spend from mortgage equity withdrawal 1991-2003

Source: BHPS