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The authors examine the impact of shocks to the value of housing wealth on household consumption and saving behavior in the UK during the 1990s, in light of the suggestions that personal sector spending and saving behavior in the UK may have become closely related to movements in house prices since financial deregulation of the housing finance industry during the 1980s.

The empirical specification used local house price variation over time from county level surveys of house prices rather than self reported values of housing wealth to avoid the danger that self reported values might be contaminated by expenditure on improvements and additions and by moving behavior, both of which are likely to correlate with measures of financial saving. In addition, to estimate the true relationship between a real house price shock and active saving, account must be made of any correlation between the housing shock and other financial components of the household balance sheet, by controlling for the effect of passive saving which occurs through the real appreciation or depreciation of financial wealth.

Regressing active saving on the initial level of real financial assets, the imputed change in financial assets, the real house price shock, and other control variables, the results imply a marginal propensity to consume of 0.028. Including an interaction term of the real housing capital gains with the initial negative equity dummy to investigate the differential impact of a shock on a household initially in negative equity (loan to house value ratio exceed unity), the results suggest that the marginal propensity to consume from real housing gains is almost three times higher for household in negative equity. As house moving by owner-occupiers may be associated with significant portfolio adjustments between housing and financial wealth, it is important to consider the question of the impact of mover-stayer selection bias in the estimates, thus reestimating the specification for nonmovers allowing for a selectivity correction term, the results show some reduction in the size and significance of real housing gain coefficients, particularly for the negative equity effect, nevertheless evidence support that owner occupiers with positive equity offset their housing gain even if they do not actually move to realize that gain.

Investigating whether there is asymmetry in behavior to nominal housing gains and losses, by estimating separate regressions for active saving in 1993-1995 when most households experienced real housing losses, and 1995-1999 when real housing losses were minimal, the results confirm that households behave differently in response to real housing gains compared to losses, as the effect of the real house price shock is statistically significant for the period of housing gains but not for losses, and the negative equity interaction effect is now strongly significant during the period of gains. For owner occupiers with positive equity the implied MPC from a positive housing wealth gain is 0.009, but for those in negative equity it is 0.044.