Policy uncertainty and precautionary saving

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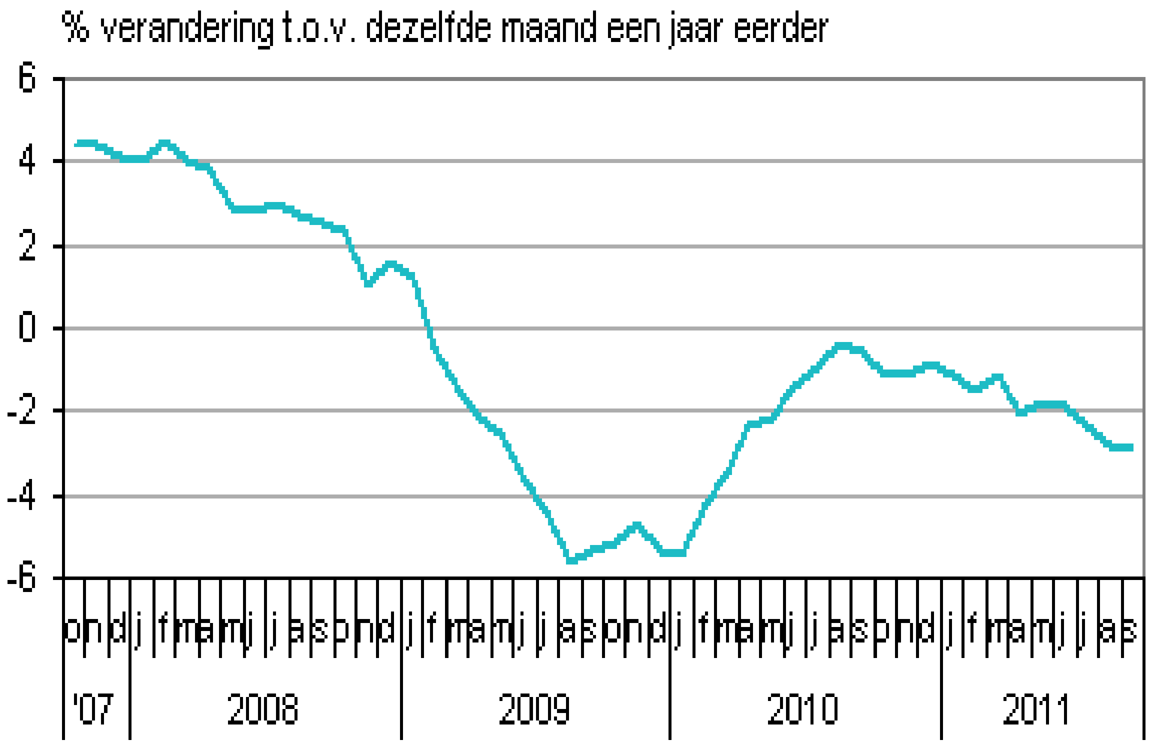
Background

- Real house prices tripled in 1985–2005
  - MID in the Netherlands is generous
  - Cheap mortgage insurance (NHG)
  - High LTVs
  - Increasing popularity of interest only mortgage
- Decrease in house prices in recent years
  - Appr. 20% in total
  - Many mortgages ‘under water’ (LTV>1)
    - Appr. 1 million households
    - Impact on mobility

Temporary recovery in 2010



Bron: CBS, Kadaster.

Policy debate

- MID was an important issue in all elections since 2000
  - Many expected a reform (DHS, figure 1)
    - Are those who ‘don’t know’ more uncertain?
- The authors fielded a questionnaire immediately after the 2010 elections

Questionnaire

- Three scenarios
  - Gradual reduction of the maximum rate
  - Gradual reduction of the maximum amount
  - Transfer to ‘box 3’ (same treatment as other assets)
- Expectations w.r.t. house price development
  - Are associated with observed local price movements
- Merged with DHS

Specification

- Starting point is Caroll and Samwick (1998)
- Ratio of active savings to permanent income is the dependent variable
  - Untransformed
  - How is permanent income measured?
- Cross-section analysis

Results

- Short term
  - No impact of aggregate (house price) uncertainty
  - Perceived house price risk of a policy reform increases savings
    - Effect 1.6%
  - If a more comprehensive control of uncertainty is used, the effect more than triples
- Long term
  - Similar result for the second specification
  - Insignficant coefficient if the more comprehensive control is used

Remarks (1)

- Your reasoning seems to be:
  - Policy reform causes house prices to change
  - Change in house prices causes a change in savings
    - Why?
      - Most people do not want to sell their house
      - House price developments are highly correlated
      - Few people sell their house at retirement
        - Perhaps their *children* should save more

Remarks (2)

- The perceived policy reforms would have consequences for net interest payments
  - They would increase for a number of years
  - This would increase ‘fixed’ expenditures
  - And reduce the opportunities for saving
- The actual reform (in 2012) did not concern existing mortgages
  - Lower house prices and low interest rates mitigated the impact on first-time buyers

Remarks (3)

- Relationship between the questionnaire and the two specifications was not clear to me
- Is the symbol μ ever explained?
- Why not do a panel data analysis?